National Energy Board

Reasons for Decision

Canadian Petroleum Association Ltd.

GH-R-1-91

June 1992

Review

National Energy Board

Reasons for Decision

In the Matter of

Canadian Petroleum Association Ltd.

Application for Review of Decision re Alberta and Southern Gas Co. Ltd. (GH-5-88)

GH-R-1-91

June 1992

© Minister of Supply and Services Canada 1992

Cat. No. 0-662-19784-4
ISBN NE 22-1/1992-10E
This report is published separately in both official languages.

Copies are available on request from:
Regulatory Support Office
National Energy Board
311 Sixth Avenue S.W.
Calgary, Alberta
T2P 3H2
(403) 292-4800

Printed in Canada

Ce rapport est publié séparément dans les deux langues officielles.

Exemplaires disponibles sur demande auprès du:
Bureau du soutien à la réglementation
Office national de l'énergie
311, 6e Avenue s.-o.
Calgary (Alberta)
T2P 3H2
(403) 292-4800

Imprimé au Canada

Table of Contents

Abbreviations 5

Glossary of Terms 7

Recital and Appearances 8

1. The Application and Pre-hearing Process 1
1.1 The CPA Application, as amended 1
1.2 The Pre-hearing Process 2
1.2.1 The Board's Hearing Order GH-R-1-91 2
1.2.2 Preliminary Matters Prior to the GH-R-1-91 Proceeding 3
1.3 The Interim Measures 5

2. Background 6
2.1 Policy Framework For Natural Gas Trade Between Canada And The United States 6
2.1.1 Trade Policy 6
2.1.2 Related Actions of National Regulatory Agencies - Open Access Transportation . . 9
2.2 The NEB Market-Based Procedure 9
2.3 The GH-5-88 Hearing 10
2.4 California Public Utilities Commission Policy on Gas Procurement and Transportation Services 11
2.4.1 CPUC and CEC Policy at the time of the GH-5-88 Proceeding 11
2.4.2 CPUC Policy after the GH-5-88 Proceeding 12

3. The GH-R-1-91 Hearing 18
3.1 Summary of Issues 18
3.2 CPA Motion 18
3.3 Issues Addressed in the GH-R-1-91 Proceeding 24
3.3.1 Issues (a) and (b) 24
3.3.2 Issue (c) 29
3.3.3 Issue (d) 31
3.3.4 Issues (e) and (f) 39
3.3.5 "Incrementality Test" 41

4. Summary and Conclusions 44

5. Decision 47

6. Disposition 49

Abbreviations

A&S	Alberta and Southern Gas Co. Ltd.
American Natural	American Natural Gas Corporation
ANG	Alberta Natural Gas Company Ltd
APMC	Alberta Petroleum Marketing Commission
B.C.	Ministry of Energy, Mines, and Petroleum Resources and Ministry of the Attorney General for the Province of British Columbia
Bcfd	billion cubic feet per day
Board or NEB	National Energy Board
Brymore	Brymore Energy Ltd.
CEC	California Energy Commission
Conwest	Conwest Exploration Company Limited
CPA	Canadian Petroleum Association
CPUC	California Public Utilities Commission
DOE	U.S. Department of Energy
DOE Guidelines	Department of Energy - New Policy Guidelines and Delegation Orders on the Regulation of Imported Natural Gas, February 1984
DRA	Division of Ratepayer Advocates of the California Public Utilities Commission
FERC	Federal Energy Regulatory Commission
FTA or Free Trade Agreement	Canada-United States Free Trade Agreement
GATT	General Agreement on Tariffs and Trade
GH-3-86 Review	Reasons for Decision In the Matter of An Application by Cyanamid Canada Pipeline Inc. Pursuant to Section 12(l) of the Act for Review of the jurisdiction contained in the National Energy Board Reasons for Decision in the Matter of an Application Under Section 49 and Subsection 59(3) of the *National Energy Board Act* of Cyanamid Canada Pipeline Inc., December 1986 GH-3-86
GHR-1-87 Decision	Reasons for Decision In The Matter of Review of Natural Gas Surplus Determination Procedures, July 1987.

GH-5-88 Decision	Reasons for Decision, Alberta and Southern Gas Co. Ltd., May 1989.
IGI	IGI Resources, Inc.
IPAC	Independent Petroleum Association of Canada
LDC	Local Distribution Company
MBP	Market-Based Procedure
MH-1-87	Reasons for Decision, Manitoba Oil and Gas Corporation Application dated 25 May 1987, as Amended, for Orders Directing TransCanada PipeLines Limited to Receive, Transport and Deliver Natural Gas and Fixing Tolls, September 1987.
Mcfd	thousand cubic feet per day
MMcfd	million cubic feet per day
NEB Act	*National Energy Board Act*
NEB Rules	draft *National Energy Board Rules of Practice and Procedure*
NOVA	NOVA Corporation of Alberta
Pan-Alberta	Pan-Alberta Gas Ltd.
Part VI Regulations	*National Energy Board Part VI Regulations*
PG&E	Pacific Gas and Electric Company
PGT	Pacific Gas Transmission Company
Poco	Poco Petroleums Ltd.
RH-1-88 Phase I	Reasons for Decision, TransCanada PipeLines Limited Decision RH-1-88 Phase I Decision, November 1988.
SPURR	School Project for Utility Rate Reduction
TransCanada	TransCanada PipeLines Limited
UEG	Utility Electric Generation
U.S.	United States
1985 Agreement	October 1985 Agreement Among the Governments of Canada, Alberta, British Columbia and Saskatchewan on Natural Gas Markets and Prices.

Glossary of Terms

A&S Producers	A group of about 190 Alberta and B.C. producers who are suppliers to A&S under long-term contractual arrangements.
Access Agreement	A settlement agreement reached in August 1990 among Canadian producers, the Government of Alberta, the gas utilities (such as PGT), independent gas marketers and California industrial and consumer advocate groups to facilitate the implementation of capacity brokering on PGT. It provides for 250 MMcfd of capacity on PGT to be made available to non-core customers for separately negotiated direct purchases of gas from individual A&S producers.
Buy/Sell Arrangement	An arrangement by which the end-user purchases its own supply of gas and arranges for transportation to a distributor's delivery point. The distributor purchases the gas and then sells it back to the end-user at a delivery point, generally the user's plant gate.
Capacity Brokering	The assignment by a shipper of its contracted transportation capacity entitlements to another shipper without the need for the consent of the pipeline company.
Core Customers	Customers with no fuel alternatives to natural gas, such as residential and small commercial customers. These customers traditionally receive gas service from gas utilities under a "bundled" service of gas supply procurement and transportation service.
Firm Service	Transportation service which provides transportation of up to a maximum daily volume without interruption except under extraordinary circumstances.
Interruptible Service	Transportation service subject to curtailment for either capacity and/or supply reasons, at the option of the pipeline company.
Noncore Customers	Customers with alternative fuel capability, such as large commercial and industrial customers, including power plants, and enhanced oil recovery customers. These customers have the option of purchasing gas from a gas utility's core or non-core portfolio or choosing to have their own gas purchases transported by the gas utility or any combination thereof.
Open Access Transportation	The non-discriminatory access to pipeline transportation services.
Self-displacement	The direct purchase of gas by Canadian LDCs to displace pipeline sales gas otherwise obtained under contract from a pipeline company.
Take-or-pay Obligation	A provision in a contract requiring that gas contracted for, but not taken, will be paid for.

Recital and Appearances

IN THE MATTER OF the *National Energy Board Act*, and the Regulations thereunder:

AND IN THE MATTER OF an application to the National Energy Board dated 29 May 1991 and subsequently amended on 27 November 1991 by the Canadian Petroleum Association requesting the Board to review its GH-5-88 Decision to issue gas export Licence GL-111 to Alberta and Southern Gas Co. Ltd.

Heard at Calgary, Alberta on 24, 25, 26, 27 and 28 February 1992 and 2, 3, 4, 10, 11 and 12 March 1992.

BEFORE:

R. Priddle	Chairman
J.-G. Fredette	Member
A.B. Gilmour	Member

APPEARANCES:

C.K. Yates	Canadian Petroleum Association
L.L. Manning	Independent Petroleum Association of Canada
M.A. Putnam, Q.C. K.F. Miller	Alberta and Southern Gas Co. Ltd.
D.G. Hart, Q.C.	Alberta Natural Gas Company Ltd.
P.H. Davies	Alberta Energy Company Ltd.
M.J. Black	Amerada Hess Canada Ltd.
C.H. Hughes	American Natural Gas Corporation
S.G. Trueman	Amoco Canada Petroleum Company Limited
T.G. Kane	ANR Pipeline Company
D.C. Edie	Brymore Energy Ltd.
J.D. Brett	Centra Gas Manitoba Inc.
R.B. Brander	Centra Gas Ontario Inc.
R.A. Pashelka	Chevron Canada Resources
J. Kalman P. Hampaul	Conwest Exploration Company Limited
G. Walsh	Czar Resources Ltd.

M. McKenzie	Esso Resources Canada
G.R. Walsh	G. R. Walsh & Associates Ltd.
J.S. Bulger	Gaz Métropolitain, inc.
M.M. Moseley	IGI Resources, Inc.
B.A. Woods	Mobil Oil Canada
L.E. Smith T.M. Sutliff	Northwest Pipeline Corporation
L.E. Smith	The Northeast Group - Joint Intervention of Alberta Northeast Gas, Limited, Boundary Gas, Inc., Ocean State Power, Ocean State Power II, Masspower, Selkirk Cogen Partners, L.P., Selkirk Cogen Partners II, L.P.
C. Havers	NOVA Corporation of Alberta
A.S. Hollingworth K.J. Warren T.N. Cotter M.E. Lipson	Pacific Gas and Electric Company
J.B.D. Malone, Q.C.	Pacific Gas Transmission Company
W.M. Smith	Pacific Interstate Transmission Company
F.F. Foran	Pan-Alberta Gas Ltd.
R.H. Mackie	PanCanadian Petroleum Limited
R.B. Hillary	Poco Petroleums Ltd.
M.D. Grant	ProGas Limited
L.E. Smith J.F. Walsh	San Diego Gas and Electric Company
J.T. Horte	Saskatchewan Oil and Gas Corporation
J.M. Dunn	Shell Canada Limited
L.G. Keough	Southern California Edison Company
A.M. Walsh	Summit Resources Limited
D. Wharton	Suncor Inc..
N.D.D. Patterson	TransCanada PipeLines Limited

M.J. Samuel	Western Gas Marketing Limited
C.W. Dehart	Williams Gas Marketing Company
W.M. Moreland	Alberta Petroleum Marketing Commission
J.T. Brett	California Public Utilities Commission
M. Tremblay J. Robitaille	Procureur général du Québec
G.R. Walsh	Ministry of Energy for Ontario
J.L. Fingarson P. Jarman	Ministry of Energy, Mines and Petroleum Resources, British Columbia / Ministry of the Attorney General, British Columbia
F.J. Morel	National Energy Board

Chapter 1
The Application and Pre-hearing Process

1.1 The CPA Application, as amended

On 27 November 1991, the Canadian Petroleum Association ("CPA") filed with the National Energy Board ("NEB" or "Board") an amended application for review of the *Board's Reasons for Decision, Alberta and Southern Gas Co. Ltd., May 1989* ("GH-5-88 Decision") pertaining to the issuance of Licence GL- 111 to Alberta & Southern Gas Co. Ltd. ("A&S") which had the effect of extending Licence GL-99 previously issued to A&S. The amended application updated CPA's earlier application for review filed with the Board on 29 May 1991.

The amended application requested that the Board take immediate action to counteract the effects of Decision 91-11-025 of the Public Utilities Commission of the State of California ("CPUC") dated 6 November 1991 relating to the CPUC's decision on rules for capacity brokering in California. The CPA requested, pursuant to the provisions of Section 21 of the Act, that the Board review its GH-5-88 Decision in light of the aforesaid action and other actions by the CPUC, all of which constituted new facts and changed circumstances which have arisen since the Board's decision in the GH-5-88 proceeding. The CPA further requested that, for this purpose, the Board immediately convene a public hearing.

In its application, as amended, the CPA specifically requested that the Board:

1. immediately vary all short-term export orders to add a condition that prohibits deliveries into the pipeline system of Pacific Gas Transmission Company ("PGT") of any Canadian gas destined for utilization in the Northern California market that is not gas presently contracted by A&S for sale to PGT. The condition should continue in full force and effect until the Board has held a hearing and made its findings and rendered its decision in respect of the CPA application;

2. immediately convene a public hearing to conduct a review of the GH-5-88 Decision in light of the changed circumstances and new facts that have arisen;

3. immediately upon completion of the public hearing:

   (a) confirm and reiterate that the continuation and extension of Licence GL-99 by Licence GL-111 were authorized by the NEB in accordance with the Market-Based Procedure in reliance upon freely negotiated long-term contracts;

   (b) direct that such long-term contracts shall govern the export of Canadian gas to the Northern California market until restructuring of those contracts is completed and all Canadian and United States regulatory tribunals have, after due process, granted all approvals necessary to allow the restructured contracts to govern; and

   (c) condition all short-term export orders to prohibit deliveries into the pipeline system of PGT of any Canadian gas destined for utilization in the Northern California market that is

not gas presently contracted by A&S for sale to PGT. The prohibition should continue until restructuring is completed and all requisite approvals have been obtained after due process; and

4. determine and declare that the actions of the CPUC since the issuance of the GH-5-88 Decision are contrary to the intent of Canadian and United States ("U.S.") energy policy, the Market-Based Procedure, the GH-5-88 Decision and the *Canada-United States Free Trade Agreement* ("Free Trade Agreement" or "FTA").

The CPA took the position that the actions of the CPUC were contrary to the GH- 5-88 Decision, the Market-Based Procedure, Canadian and U.S. energy policy and the Free Trade Agreement. It was also the position of the CPA that the CPUC Decision 91-11-025 violated the sanctity of the contracts upon which the Board based the GH-5-88 Decision. For this reason, the CPA submitted that the Board should take immediate action to neutralize the concerted regulatory effort of the CPUC to frustrate the freely-negotiated contractual undertakings upon which the GH-5-88 Decision was based. As outlined above, the CPA contended that this action should include the immediate variation of all short-term export orders that permit deliveries on the PGT system that undermine the Pacific Gas and Electric Company ("PG&E")/PGT/A&S/A&S producer contracts and should also include the conditioning of short-term orders to prevent the frustration of the GH-5-88 Decision until such time as restructuring has taken place and the restructured contracts have received regulatory approval after due process.

1.2 The Pre-hearing Process

1.2.1 The Board's Hearing Order GH-R-1-91

The Board's decision to hold a public hearing to review the GH-5-88 Decision was in response to the amended application for review filed by the CPA on 27 November 1991.

In addition to the application for review as amended, the Board considered the comments of interested parties which it had previously solicited in respect of CPA's original application. The Board concluded that a review of its GH-5-88 Decision was warranted on the basis of new facts and changed circumstances relating to the recent actions of the CPUC which could have severe detrimental effects on the Canadian public interest.

Therefore, the Board decided on 12 December 1991, pursuant to sections 12, 21 and 59 of the *National Energy Board Act* ("NEB Act") to hold a public hearing and issued Hearing Order GH-R-1-91 on 19 December 1991 to review A&S' gas export Licences GL-99 and GL-111, the Board's GH-5-88 Decision, and inquire into the following issues:

a) the effects of the regulatory actions and decisions taken in California on existing and proposed exports of Canadian gas authorized by the Board under Licences GL-99 and GL-111;

b) the consequences of these actions and decisions on the Board's findings and decision in GH-5-88 which were rendered under the Board's Market-Based Procedure;

c) the likelihood of commercial restructuring of the long-term contractual arrangements underpinning the export licences in view of these actions and decisions and, if such restructuring is to occur, the appropriate period of time for it to take place;

d) whether it is permissible within the Board's current authority and, if so, whether it is desirable for the Board to attach a condition to all short-term export orders that would prohibit exports at Kingsgate, British Columbia, of any Canadian gas destined for utilization in the Northern California market that is not gas presently contracted by A&S for sale to PGT and, if so, for what period of time should such a condition remain in effect;

e) whether access to pipeline capacity on Alberta Natural Gas Company Ltd ("ANG") does or should take into account existing long-term contractual arrangements for the sale of Canadian gas to California markets in view of the potential consequences of recent regulatory actions and decisions taken in the United States of America; and

f) whether amendments to ANG's tariff are required to address those issues raised in paragraph e) or any other effects on the transportation and sale of Canadian gas as a result of the regulatory actions and decisions taken in the United States of America and, if so, for what period of time should the changes to the tariff remain in effect.

By Hearing Order GH-R-1-91, the Board also sought the views of interested parties on whether interim measures, to ensure that exports to California under long-term licences on the ANG pipeline were not displaced by exports under short-term orders, were permissible within the Board's current authority and, if so, whether any should be implemented, pending the outcome of the GH-R-1-91 public hearing. The measures considered by the Board were:

1) to immediately vary all short-term export orders to add a condition that prohibits deliveries at Kingsgate, British Columbia of any Canadian gas for utilization in the Northern California market that is not gas presently contracted by A&S for sale to PGT; and/or

2) to suspend any portion of ANG's tariff and to substitute therefor provisions which would address immediately access to firm and interruptible transportation, assignment or brokering of capacity and other terms and conditions of transportation service on the facilities of ANG.

1.2.2 Preliminary Matters Prior to the GH-R-1-91 Proceeding

ANG, PG&E and PGT would be filing written evidence and presenting witnesses to be cross-examined at the public hearing. The CPA submitted that "the best evidence on the issues to be considered by the Board in the public hearing was available from the major participants in the proceedings and activities that have created the new facts and changed circumstances which have arisen since the GH-5-88 Decision was rendered." Furthermore, the CPA proposed that the evidence of these companies take place before any other intervenors were required to appear for cross-examination. In the event that any of the four companies would not provide evidence, the CPA indicated that it was prepared to make immediate application to the Board for an order directing that such evidence be obtained and that witnesses be made available for examination. The CPA also requested that the Board invite the CPUC to participate in the oral portion of the GH-R-1-91 proceeding since the CPUC's decisions, according

to the CPA, have been contradictory to its position in the GH-5-88 proceeding, and contrary to the GH-5-88 Decision and the Market-Based Procedure.

In response to the CPA's letter dated 15 January 1992, the Board sent letters to A&S, ANG and the CPUC dated 23 January 1992. The letters addressed to A&S and ANG advised the companies that the Board expected them to file evidence and have witnesses available for cross-examination, given the potential impact that any decisions of the Board, as a result of the GH-R-1-91 proceeding, could have on Licences GL-99 and GL-111 and the ANG pipeline facilities respectively. Furthermore, the Board indicated that it would expect A&S and ANG to produce witnesses from affiliated companies, if necessary in their judgement. The Board's letter to the CPUC stated that there were no obstacles to the CPUC participating in the proceeding and informed the CPUC that any witness who might appear on its behalf should have full and unequivocal authority to address issues related to Canadian gas sales to California.

In a letter dated 23 January 1992, the Board provided the CPA with a copy of the letters from the Board addressed to A&S, ANG and the CPUC. The Board noted, in its letter, that PG&E and PGT were outside its jurisdiction and, therefore, the decision whether to offer evidence and to provide witnesses was a matter for these parties to decide. With respect to the conduct of the hearing, the Board informed the CPA of its intention to hear, in order of appearance, the CPUC (should it choose to present evidence), CPA, A&S, ANG and other interested parties.

In a letter dated 30 January 1992, the CPA maintained its position that evidence of PGT and PG&E was essential to the GH-R-1-91 hearing and that it would take steps to seek an order compelling the attendance of witnesses from these companies, should they choose not to file evidence and produce witnesses directly or through A&S and ANG. With respect to the order of appearances, the CPA suggested that the Board hear first witnesses from A&S, as it was the applicant in the GH-5-88 proceeding and the licence-holder, then PG&E, PGT and ANG followed by all other interested parties.

In reply to the CPA's letter dated 30 January 1992, the Board confirmed, by a letter dated 5 February 1992, its previous position with respect to the participation of PG&E and PGT and the conduct of the oral portion of the hearing, as expressed in its letter of 23 January 1992 to the CPA. The Board considered the CPA to be the applicant and, therefore, expected the Association to present its evidence first. The Board also stated that if the CPA were to seek an order compelling the attendance of witnesses from PG&E and PGT, the Board would address the matter at the appropriate time.

In a letter dated 7 February 1992, the CPA asked the Board to confirm that the GH-R-1-91 proceeding, which was a review of the GH-5-88 Decision and proceeding, would include the entire record of the GH-5-88 proceeding or alternatively, that the Board would grant leave pursuant to Section 21 of the draft *National Energy Board Rules of Practice and Procedure* ("NEB Rules") to receive in the GH-R-1-91 proceeding the entire record of the GH-5-88 proceeding. In addition, the CPA requested that the Board indicate that a copy of the GH-5-88 proceeding was available for viewing at the offices of the Board and that reproduction and service of copies on interested parties to the GH-R-1-91 proceeding was not required.

In a letter dated 13 February 1992 to the CPA, the Board directed that it was not necessary to receive the GH-5-88 record into the GH-R-1-91 proceeding pursuant to Section 21 of the draft NEB Rules. Furthermore, the Board indicated that the GH-5-88 record was available for viewing in the Board's

Library and that the CPA was not required to provide a copy of that record to interested parties to the GH-R-1-91 proceeding.

1.3 The Interim Measures

After having considered the submissions of intervenors and the replies of the CPA, A&S and ANG on the proposed interim measures enunciated in the GH-R-1-91 Hearing Order, the Board issued two interim orders on 4 February 1992. Order MOI-1-92 required any company planning to export additional natural gas at Kingsgate, British Columbia and potential applicants for short-term export orders for the same export point to obtain prior permission of the Board. The Board also issued Order TGI-1-92 which suspended the right of shippers on ANG to release or transfer any portion of their firm capacity on the ANG pipeline system.

The Board concluded that the interim measures were necessary because of the potentially detrimental effects of recent regulatory actions by the CPUC on the Canadian public interest. These interim measures were to remain in effect until the completion of the public hearing, at which time the Board would determine whether the interim orders should be made final or whether any other orders should be issued.

Chapter 2
Background

This chapter outlines the circumstances under which a licence extension was issued to A&S in 1989 and the subsequent changes in those circumstances, particularly those resulting from CPUC actions, which are relevant to this proceeding. Section 2.1 reviews the gas trade policy and the regulatory environment at the federal level in Canada and the U.S. that existed immediately prior to the proceeding held pursuant to Hearing Order GH-5-88. Section 2.2 describes the Market-Based Procedure, adopted by the Board in 1987 as a basis for determining whether to approve applications for licences to export natural gas. Section 2.3 reviews the evidence heard during the GH-5-88 proceeding related particularly to the supply and transportation arrangements and the Northern California market to be served by the proposed export. Finally, Section 2.4 provides a review of the California regulatory policy which existed at the time of the GH-5-88 proceeding and the subsequent changes in that environment which began shortly after the Board's GH-5-88 Decision was rendered in May 1989.

The above referenced supply and transportation arrangements relate to the chain of contracts between Canadian producers, A&S, ANG, PGT and PG&E. A&S buys gas from Canadian producers and exports it to PGT at the Kingsgate, British Columbia export point for sale and delivery to PG&E. A&S, a wholly owned affiliate of PG&E, purchases the gas under long-term contracts from producers in Alberta and British Columbia. The gas from British Columbia is transported on the Westcoast Energy Inc. pipeline system into the NOVA Corporation of Alberta ("NOVA") pipeline system in Alberta. The Alberta and British Columbia gas is transported on the NOVA facilities for delivery to the pipeline facilities of ANG near Coleman, Alberta. ANG transports the gas under a firm transportation contract with A&S across southeastern British Columbia for sale and delivery by A&S to PGT at the international boundary near Kingsgate, British Columbia.

PGT, a wholly-owned affiliate of PG&E, transports the gas across the states of Idaho, Washington and Oregon for sale and delivery to PG&E at the Oregon-California border near Malin, Oregon. PG&E, a combined gas and electric utility, then transports and sells the gas to its customers throughout Northern California including its major load centres in Sacramento and San Francisco.

This background summary is based on evidence filed in various proceedings before the Board, including the GH-R-1-91 proceeding, in California proceedings and in public documents.

2.1 Policy Framework For Natural Gas Trade Between Canada And The United States

2.1.1 Trade Policy

The NEB's GH-5-88 proceeding, which resulted in the extension of Licence GL-99 by the issuance to A&S of a long-term licence to export gas to the Northern California market, took place after governments and regulators in Canada and the U.S. had put in place a new natural gas trade policy framework.

The current framework of Canadian natural gas policy, at both the federal and producing-province level, and relating to both domestic and export sales, is set out in the October 1985 *Agreement Among the Governments of Canada, Alberta, British Columbia and Saskatchewan on Natural Gas Markets and Prices* ("the 1985 Agreement"). These governments agreed that "... a more flexible and market-oriented pricing regime was required for the domestic pricing of natural gas" and the intent of this agreement was "... to create the conditions for such a regime, including an orderly transition which is fair to consumers and producers and which will enhance the possibilities for price and other terms to be freely negotiated between buyers and sellers." (1985 Agreement, p. 1, paragraph 1.)

With respect to exports, the following criteria act as guidelines for gas export contractual arrangements:

1. The price of exported natural gas must recover its appropriate share of the cost incurred.

2. Export contracts must contain provisions which permit adjustments to reflect changing market conditions over the life of the contract.

3. Exporters must demonstrate that export arrangements provide reasonable assurances that contract volumes will be taken.

4. Exporters must demonstrate that the producers supplying gas for an export project endorse the terms of the export arrangements and any subsequent revisions thereof.

Clause 16 of the 1985 Agreement anticipated that the Board would review its surplus determination procedures for the export of natural gas:

> The governments anticipate that reviews of surplus tests underway or shortly to be initiated by the National Energy Board and by the appropriate provincial authorities will result in significantly freer access to domestic and export markets and thus will contribute to the achievement of the market-oriented pricing system contemplated in this Agreement.
>
> (1985 Agreement, p. 3)

In 1987, the Board, in its *Reasons for Decision In The Matter of Review of Natural Gas Surplus Determination Procedures, July 1987* ("the GHR-1-87 Decision") adopted a new procedure, the Market Based Procedure, for regulating exports of gas under long-term licences. (See section 2.2)

At the same time, in the United States, the emerging policy, as expressed in the Department of Energy *New Policy Guidelines and Delegation Orders on the Regulation of Imported Natural Gas* ("DOE Guidelines") of February 1984, was designed to establish international natural gas trade on a market competitive basis and provide for the market, not governments, to determine the price and other contract terms of imported gas. The DOE Guidelines state:

> ... the guidelines establish a regulatory framework for buyers and sellers to negotiate contracts based on traditional competitive and market considerations, with minimal regulatory interference.
>
> (DOE Guidelines, p.2)

The guidelines also contain such criteria as:

- the terms and conditions of the gas purchase contract, taken together, must provide a supply of gas that the importer can market competitively over the term of the contract;

- contracts should also contain provisions to protect the parties in the event of changes in the circumstances in which the contract is expected to operate, and to permit contractual adjustments in such circumstances;

- import agreements should provide a competitive energy source for the duration of the import;

- need for imported gas will be addressed in terms of marketability of the proposed import, thus if the gas is competitive in the proposed market area and, through its contract terms, will remain competitive throughout the contract period then the rebuttable presumption exists that the gas is needed in that market; and

- the security of gas supply and its transportation to the U.S. border remain important components of the public interest especially those under long- term arrangements, thus larger volume and longer time period imports must demonstrate greater reliability of supply than smaller scale imports for a shorter time period.

(DOE Guidelines, p. 19-22)

As indicated, these are guidelines for U.S. buyers in negotiating their contractual arrangements with a view to obtaining the necessary import approvals.

The DOE Guidelines state that:

> The market, not government, should determine the price and other contract terms of imported gas. U.S. buyers should have full freedom...along with the responsibility ... for negotiating the terms of trade arrangements with foreign sellers.
>
> (DOE Guidelines, p. 6)

and that:

> The government, while ensuring that the public interest is adequately protected, should not interfere with buyers' and sellers' negotiations of the commercial aspects of import arrangements. The thrust of this policy is to allow the commercial parties to structure more freely their trade arrangements, tailoring them to the markets served.
>
> (DOE Guidelines, p. 7)

It also states that:

> This policy approach presumes that buyers and sellers, if allowed to negotiate free of constraining governmental limits, will construct competitive import agreements that will be responsive to market forces over time.
>
> (DOE Guidelines, p. 14)

Thus, the international gas trade policies that were in place in both Canada and the United States at the time of the OH-5-88 proceeding provided and, indeed, created a competitive, market-oriented framework for commercial negotiation.

2.1.2 Related Actions of National Regulatory Agencies - Open Access Transportation

The new policies in Canada and the U.S. were reflected in measures taken by the Federal Energy Regulatory Commission ("FERC") and the NEB to provide access to pipelines so that buyers could access gas supply and sellers could access markets.

The FERC Order 436 and Order 500 initiated the segregation of the merchant from the transportation function on U.S. interstate pipelines. This process continued with the release of Order 636 by FERC on 8 April 1992.

The NEB, in decisions related to the operations of TransCanada PipeLines Limited ("TransCanada"), acted to remove restrictions on access to the TransCanada system so that non-discriminatory access would be available to any party wishing to use it. *(Reasons for Decision, TransCanada PipeLines Limited Availability of Services, May 1986 and Reasons for Decision, TransCanada PipeLines Limited RH-1- 88 Phase I Decision, November 1988* ("RH-1-88 Phase I Decision").

Over time, open access transportation has been implemented on all the major pipelines regulated by the FERC in the U.S. and by the Board in Canada.

2.2 The NEB Market-Based Procedure

Pursuant to Section 118 of the NEB Act, the Board is required to ensure that natural gas proposed to be exported is surplus to reasonably foreseeable Canadian requirements. In July 1987, the Board, in its GHR-1-87 Decision, adopted a new surplus determination procedure - the Market-Based Procedure ("MBP") - based on "the premise that the market will generally operate in such a way that Canadian requirements for natural gas will be met at fair market prices." (p.24)

The MBP consists of three components: a complaints procedure; an export impact assessment; and a public interest determination. The complaints procedure seeks to ensure that Canadian users are able to obtain supplies of gas under contract on terms and conditions, including price, similar to those in the export arrangement. The export impact assessment allows the Board to determine whether a proposed export is likely to cause Canadians difficulty in meeting their energy requirements at fair market prices. The public interest determination includes an assessment of all other factors the Board considers to be relevant in determining the public interest. Among other factors are the evidence on the adequacy of the gas supplies available to the export licence applicant to support the applied-for volumes over the requested licence term; the nature of the contractual arrangements; the support by producers for the proposed export; evidence that export volumes will be taken; that the export revenues will recover the costs incurred; the availability of pipeline space; and information on any relevant government policies or positions.

2.3 The GH-5-88 Hearing

In 1987, A&S applied for an amendment to its export Licence GL-99 to extend the term of the licence by 16 years from 1994 to 2010 and to increase the term quantity by six trillion cubic feet. The Board conducted a public hearing pursuant to Order GH-5-88 to deal with the application in December 1988.

In the GH-5-88 proceeding, the Board used its Market-Based Procedure and considered a number of public interest factors, including the applicant's gas supply and transportation arrangements and the markets to be served by the proposed export.

A key issue during the proceeding was the extent of the reliance by A&S upon supply under development contracts, particularly in the later years of the licence requested. As defined in the Board's GH-5-88 Decision, a development contract is one in which not all gas reserves are established at the time the contract is executed. The contract provides for the timely development of potential reserves and assures the producer of a market for its future gas production. In discussing its reliance on development contracts, A&S argued that the strong California market would provide producers with enough incentive to make the investments necessary to develop the gas needed to meet the requirements of that market. The development of the new gas supplies to serve the California market would also require investments in new pipeline facilities. A&S estimated that about $100 million in additional Canadian facilities would be necessary to transport the proposed export volumes.

The evidence presented in the proceeding established that Canadian gas had traditionally provided about 40 percent of PG&E's total system supply and over 50 percent in the late 1980s because of El Paso Natural Gas Company's inability to price long-term supplies competitively. At the proceeding, A&S also stated that historically high rates of take for its gas, the competitive terms and conditions of its contract with PGT, the equitable purchase provisions between PG&E and PGT, and the forecast long-term growth for PG&E's market were strong arguments for an extension of its licence. In addition, the evidence was that the international gas sales contract between A&S and PGT provided for periodic review of the commodity rate paid to A&S to ensure that the price remained competitive with the price of major competing energy sources in the market of PGT's customer, PG&E. As well, the contract contained a 50 percent take-or-pay provision and required PGT to take gas from A&S on the same equitable percentage basis as specified in the PG&E/PGT Service Agreement so long as Canadian gas was competitively priced.

At the proceeding, PG&E presented argument for the approval of the full applied- for licence term. PG&E testified that Canadian gas would have a key role in its new supply portfolio and that Canadian gas would undoubtedly continue to be a foundation of its supply base. PG&E also stated that the CPUC and the California Energy Commission ("CEC") supported the concept of a long-term supply commitment from Canada.

After considering all the evidence, the Board concluded that the Northern California market was a proven and highly dependable market for Canadian gas and concurred with A&S that competitively priced gas supplies from Canada would likely continue to play a vital role in satisfying PG&E's market demand.

The Board determined that the issuance of a new licence to A&S would be in the public interest but, in view of the heavy reliance upon supply from development contracts in the later years of the licence

term requested, the Board decided to extend Licence GL-99 by issuing a new Licence GL-111 for a term of 11 years to 2005, five years shorter than the requested term.

2.4 California Public Utilities Commission Policy on Gas Procurement and Transportation Services

2.4.1 CPUC and CEC Policy at the time of the GH-5-88 Proceeding

The CPUC and the CEC filed letters with the Board in the GH-5-88 proceeding supporting the extension of Licence GL-99 and endorsing the concept of a long- term supply commitment from Canada. The CPUC letter of 21 October 1988 stated:

> Because of its reliability, stability and current competitiveness, the Alberta and Southern supply has allowed PG&E to assemble a gas supply portfolio which is very competitive under the market-driven regulatory framework the CPUC has encouraged. The reliability and market responsiveness of the Alberta and Southern supply are important today and give that supply an equally important role in California's gas supply future. Extending the export licence for Alberta and Southern to the year 2010 is needed to make this future role a reality. The extended export licence will assure an additional sixteen year supply of gas at a time of difficult transition in California markets. This will benefit both California gas consumers and Canadian interests by offering greater certainty of the future opportunities for this Canadian supply in PG&E's market.

In the same letter, the CPUC expressed strong support for the continuation of the A&S supply:

> For our part, my fellow Commissioners and I wish to assure the Board of the CPUC's continued desire that Alberta and Southern remain a major supplier of energy for California both in the near term and for many years to come, and of our equally continued desire to work closely with the National Energy Board to achieve that objective.

At the same time, the CEC filed a letter dated 27 October 1988 in the GH-5-88 proceeding wherein it stated:

> ...the continued availability of Canadian gas under the Alberta & Southern license is critical to PG&E and its customers.
>
> As gas markets have become more competitive in California over time, Alberta & Southern has been able to remain an extremely market responsive supply mix, without any compromise in the reliability of supplies. As we plan for future supplies to meet California's demand for diversity, reliability, and price competitiveness, we would like to continue to look to Canada. Extension of Alberta & Southern's export license to 2010 will offer greater certainty to Canadian interests of Canada's role in providing long run supplies to California and allow PG&E and California regulators to be similarly assured.

Thus, the policy in California at the time of the GH-5-88 proceeding was one that saw the A&S supply as a reliable, stable and competitive source of long- term gas supply to serve the California market.

2.4.2 CPUC Policy after the GH-5-88 Proceeding

Since the GH-5-88 Decision, issued in May 1989, the CPUC opinion of the A&S gas supply has changed: in late 1988 it viewed A&S' supply as a reliable, stable and competitive gas supply for PG&E that was to be relied upon to meet California's market requirements; in mid-1990 its view was that PG&E had entered into contract obligations which "preclude competitive access"; where the contract prices are seen to be "substantially higher than Canadian market prices"; and PG&E was instructed to renegotiate its A&S producer contracts to "provide for reduced minimum takes and improved flexibility".

In a series of decisions flowing from proceedings initiated by the CPUC - *Order Instituting Rulemaking into natural gas procurement and reliability issues* (R.88-08-018, 10 August 1988) and *Order Instituting Rulemaking on the Commission's own motion to change the structure of gas utilities' procurement practices and to propose refinements to the regulatory framework for gas utilities* (R.90-02-008, 2 February 1990) - the CPUC embarked on a regulatory policy dramatically different from that which was in place at the time of the GH-5-88 proceeding.

Decision 90-07-065 dated 18 July 1990 ("Contract Renegotiation Decision")

In Decision 90-07-065, the CPUC stated that it expected PG&E to renegotiate the A&S contracts by 31 December 1991 because the CPUC suspected that PG&E's contract prices were substantially higher than Canadian market prices. The Decision stated that the renegotiated contracts should provide for "reduced minimum takes and improved flexibility" and placed responsibility for the cost of the existing contract obligations on PG&E shareholders subject to the Commission's next reasonableness review. Although the Utility Electric Generation ("UEG") departments of the combined gas and electric utilities (such as PG&E) had been purchasing all of their gas requirements from the combined utilities' gas supply portfolio, the Decision proposed to limit such UEG purchases to 15 percent of the UEG's annual requirements from the combined utilities. Further, the Decision proposed that California customers who wished to move gas over PGT would engage in buy/sell arrangements for gas supplies from A&S until PG&E's minimum contract obligations were fulfilled. On page 31 of its Decision 90-07-065, the CPUC stated:

> Under the rules we propose in today's order, customers wishing to move gas over PGT would engage in buy/sell arrangements for gas supplies from A&S contracts until PG&E's minimum contract obligations are fulfilled in each purchase period defined in the contracts (that is, if minimum takes are on a monthly basis, non-core customers must purchase under the A&S contracts until minimum requirements are fulfilled for the month).
>
> We reluctantly propose that customers must purchase from PG&E's brokering affiliate in recognition that PG&E has contract obligations which may be binding over the short term. This circumstance thwarts efforts to increase competition for Canadian gas. For several years, we have sought to move the gas industry in the direction of more competition. During this period, PG&E appears to have done little to relieve itself of

> contract obligations which stifle efforts to increase access to Canadian supplies and which may keep prices high for all customers.
>
> Because PG&E has entered into contract obligations which preclude competitive access to bottleneck facilities, and because we suspect the contract prices are substantially higher than Canadian market prices, we expect the A&S contracts to be renegotiated. Renegotiated contracts should provide for reduced minimum takes and improved flexibility. Consideration for these concessions shall not be higher prices to core customers. Contract renegotiation should be complete by December 31, 1991. After that time, we will be predisposed to allocating to PG&E's shareholders the costs of existing contract obligations which ratepayers would otherwise bear or which would require continued purchases by non-core customers from A&S. In any event, the price PG&E pays for Canadian gas will be subject to scrutiny in PG&E's next reasonableness review.

The CEC wrote a letter dated 20 August 1990 to the CPUC stating:

> Regarding PG&E's purchases of Canadian gas, we interpret the proposed decision's language directing PG&E to renegotiate its Canadian gas contracts to mean that PG&E should renegotiate contract prices and terms at their scheduled dates and not to mean that PG&E should seek to unilaterally modify existing contracts. ... We do not support the abrogation of existing contracts.

In attempting to adapt to this Decision, Canadian producers, the Government of Alberta, the gas utilities (including PG&E), independent gas marketers and California industrial and consumer advocate groups reached an agreement to provide California end-users access to transportation on PGT and direct access to Canadian gas supplies. This agreement, known as the "Access Agreement", would allow, among other things, the reservation of up to 250 MMcfd of PGT capacity to allow PG&E's non-core customers (i.e. customers with alternative fuel capability, such as large commercial and industrial customers including power plants and enhanced oil recovery customers) to purchase gas directly from A&S producers up to 1 August 1994 and from any gas suppliers after that date. The intent of the Access Agreement was to allow time for restructuring the long-term contracts upon which the Board had based its GH-5-88 Decision.

Decision 90-09-089 dated 25 September 1990 ("Gas Procurement and Transportation Decision")

In this Decision, the CPUC adopted a settlement among interested parties to its gas procurement and transportation services proceedings to facilitate direct purchases and transportation access by California end-users, primarily non-core customers. This Decision amended the proposal in the Contract Renegotiation Decision with respect to the 15 percent limit on UEG purchases. It directed the UEG departments of combined utilities to limit their purchases from the utility system gas supply to 65 percent of their demand requirements.

In this Decision, the CPUC "applauded" the Access Agreement noted above as an effective means to implement its rules: In particular, on page 66 of the Decision, the CPUC stated:

> We agree with DRA [Division of Ratepayer Advocates] that these Settlement provisions would mitigate liability of PG&E affiliates to which ratepayers owe no particular obligation. PGT's contractual obligations to A&S are, like A&S' obligations to Canadian producers, not guaranteed by PG&E's ratepayers.
>
> On the other hand, we seek to make the best out of a difficult set of circumstances. We cannot order PGT or A&S to make capacity available for non-core customers or to renegotiate their contracts because they are not within our jurisdiction. More important, some compromise appears necessary to maintain good trade relationships with Canada, relationships which will benefit Canadians and Californians alike. For this reason, we will adopt the Settlement provisions which would be in effect until August 1, 1994.
>
> We note that PG&E informed the Commission, by way of a letter dated September 20 (Attached as Appendix B), that it has reached an agreement with A&S and APMC which provides details for implementing the non-core gas purchases from A&S producers anticipated by the Settlement. The letter's provisions appear fully consistent with the Settlement provisions incorporated into the rules we adopt today. While we cannot formally adopt this supplementary agreement as it respects matters under the jurisdiction of Canadian authorities, we do applaud the agreement as an effective means to implement the rules we adopt today.
>
> Noncore transportation customers may transport Canadian gas over PGT subject to the following conditions. Until August 1, 1994, non-core customers may negotiate gas supply arrangements only with producers under contract with Alberta and Southern (A&S). Once a non-core customer has made such an agreement with an A&S supplier, PG&E will arrange to have the gas purchased by A&S under existing gas purchase agreements and will arrange to have the gas transported by PGT. Non- core customers may purchase gas from any Canadian supplier after August 1, 1994.

In subsequent decisions, the CPUC has argued that the rules in Decision 90-09-089 were only interim provisions until a capacity brokering program was implemented.

Decision 91-02-040 dated 21 February 1991("SPURR Decision")

In respect to a proposal initiated by the School Project for Utility Rate Reduction ("SPURR"), the CPUC in this Decision approved rules to permit core customers of California (i.e. customers without dual-fuel burning capacity, such as residential and small commercial users) to aggregate their loads so that such customers could procure and transport their own gas.

In this Decision, the CPUC changed its position on the Access Agreement: "... the agreement in question has not been the subject of formal review in this or any other Commission proceeding. Although the agreement is attached as an Appendix to D.90-09-089, the Commission did not formally approve it." (p.7) Implementation of the SPURR Decision was to be immediate and would override the Access Agreement. Moreover, the CPUC stated on page 20 of Decision 92-02-042 that "... if there were PG&E liability and damages, there is no record on the issue of whether such damages are solely the result of Commission regulation and not the result of the operation of economic forces in the market place. The latter occurrence is not compensable".

Proposed Decision of Administrative Law Judge Malcolm dated 19 August 1991 ("Malcolm Decision")

Views on the rules for the implementation of capacity brokering (ie. the assignment by a shipper of its contracted transportation capacity entitlements to another shipper without the need for the consent of the pipeline company) on California intrastate pipelines, including PG&E, were heard under Administrative Law Judge ("ALJ") Malcolm. In the ALJ's proposed decision on capacity brokering submitted to the CPUC, the ALJ found that PG&E has no contractual obligations which would preclude access by other shippers over PGT; rejected the submissions of the CPA, the Independent Petroleum Association of Canada ("IPAC"), and the Alberta Petroleum Marketing Commission ("APMC") that the contracts between A&S and Canadian producers should be honoured; found that A&S has committed to contract obligations in contravention of CPUC policy; refused to honour the Access Agreement which had previously been applauded by the CPUC; and criticized the absence of the international contracts from the CPUC record.

At the proceedings, certain parties sought to exclude any evidence of the PG&E/PGT/A&S/ A&S producer chain of contractual commitments and the ALJ indicated that little weight would be given to such evidence. The ALJ also refused a request by the CPA to have PG&E, PGT and A&S witnesses testify during the hearing.

The CEC wrote a letter dated 7 October 1991 to the CPUC regarding the Malcolm Decision stating:

> While we share the PUC's ultimate goal of achieving open access and competition for Canadian gas supplies, I disagree with the proposed means of achieving that goal. The Proposed Decision's overly aggressive approach to restructuring PG&E's Canadian gas supply arrangements may very well backfire, costing California ratepayers more money and risking the security of the gas supply. Instead, the PUC should continue to allow all parties involved to freely renegotiate the existing supply contracts between Canadian producers and Pacific Gas and Electric Company's wholly owned subsidiary, Alberta and Southern ("A&S") within the framework of the 1990 "Access Agreement".

The letter went on to remind the CPUC of both Commissions' representations to this Board:

> Canada represents a stable, long-term source of economical and abundant gas supplies. It was with this long term view in mind that the President of the CPUC and the Chairman of the Energy Commission wrote to the Canadian National Energy Board ("NEB") in 1988 to recommend the extension of the A&S natural gas export license until 2005. ...
>
> Partly on the basis of these representations, the NEB approved the A&S export license. As a result, Canadian producers have made substantial investments in plant and equipment to serve the long-term California market. As we finally near the completion of a process that promises to bring substantial new interstate pipeline capacity to both Canada and the Rockies, it is critical that California does not jeopardize the long-term gas supplies that would be shipped through those pipelines by taking precipitous regulatory actions to disrupt the flow of gas from Canada. Just because today's spot market prices happen to be lower than long-term contract prices does not mean that these contracts can be easily changed overnight. Bilateral and mutual restructuring of

these contracts takes time. There is no evidence in the record that the August 1, 1994 deadline for restructuring provided under the Access Agreement is unreasonable.

PG&E Application 91-04-003 Filed 1 April 1991 ("Reasonableness Review")

On 1 April 1991, PG&E filed for authority to adjust its electricity rates effective 1 November 1991, to adjust its gas rates effective 1 January 1992 and for a CPUC order finding that PG&E's gas and electric operations during the reasonableness review period from 1 January 1990 to 31 December 1991 were prudent.

On 16 September 1991, the Division of Ratepayer Advocates ("DRA") of the CPUC filed its *Report on the Reasonableness of Gas and Electric Operations* of PG&E in proceeding 91-04-003; it sought to have the Commission direct PG&E to refund to its ratepayers approximately $392 million for the three-year period from 1988 to 1990. The DRA alleged that:

> PG&E's actions in purchasing 100% of its supplies from A&S under relatively high priced, long-term contracts were inexcusable and unreasonable. DRA estimates that, had PG&E purchased 50% of its supplies at Alberta Market Prices, it would have saved its electric and gas rate payers $392 million over the three year Record Periods.

Decision 91-11-025 dated 6 November 1991 ("Capacity Brokering Decision")

For the most part, the CPUC adopted ALJ Malcolm's Decision on capacity brokering. In the final decision, the Commission:

- directed PG&E to implement full capacity brokering on PGT by 1 October 1992 or within 60 days of a FERC rehearing order authorizing capacity brokering whichever is later, regardless of any contractual arrangements entered into by PG&E through its subsidiary PGT and A&S;
- postponed consideration of any possible restructuring costs to future CPUC gas cost reasonableness proceedings;
- disavowed the Access Agreement; and
- ordered UEGs to reduce to 50 percent for the next two years their purchases of gas supplies from the combined utilities such as PG&E, to 25 percent in the following two years and to zero in the fifth year.

With respect to potential damages to PG&E and other parties, including A&S' Canadian producers, the CPUC stated in the Decision (p. 38/9):

> With this deadline for implementation of capacity brokering, we are not requiring PG&E to resolve by a certain date any litigation against it or its affiliates brought by Canadian producers. However, we will not allow obstacles within our control to complete competition and open access between Canada and Northern California to persist. Therefore, regardless of the status of any settlements or litigation in Canada, our decision today puts PG&E on notice that as of October 1, 1992, or within 60 days

of the FERC order on rehearing authorizing capacity brokering on PGT, whichever is later, PG&E can no longer restrict access to California on the PGT line.

Also, at page 33 of the Decision, the CPUC stated that:

> ... The record in this proceeding demonstrates that A&S has contractual obligations to Canadian producers and that PGT has contractual obligations to A&S. The record provides no evidence that PG&E has legal obligations to purchase gas from any Canadian producer or A&S. PG&E therefore has failed to prove the existence or terms of contractual obligations which preclude access over PGT.

Requests for a rehearing by several parties were subsequently denied by the CPUC on 10 February 1992.

Resolution G-2967 dated 6 November 1991 ("Resolution G-2967")

Since the SPURR Decision in February 1991, PG&E had not offered buy/sell arrangements at Malin, Oregon for California core customers. Thus, as part of the Capacity Brokering Decision, the Commission ordered PG&E to:

- convert some of its firm sales rights to firm transportation rights on PGT up to the amount needed to transport core aggregation volumes in order to provide core aggregators access to Canadian supplies;
- purchase gas arranged for by the core aggregation customers and their agents and transport it for delivery in California ; and
- offer this service on a nondiscriminatory basis and not restrict this service to the purchase of gas from producers with contracts with A&S.

In February 1992, gas commenced moving on PGT pursuant to the requirements of Resolution G-2967.

Chapter 3
The GH-R-1-91 Hearing

3.1 Summary of Issues

The CPA application, as discussed in section 1.1, asked the Board to make certain declarations with respect to the Board's GH-5-88 Decision, to hold a public hearing and to take some measures to counteract the CPUC's recent actions and decisions.

The Board determined that new facts and changed circumstances warranted a public hearing.

The Board decided, on 19 December 1991, to hold a public hearing to review its GH-5-88 Decision and to inquire into certain issues identified in the Board's Hearing Order and which are listed in section 1.2.1.

3.2 CPA Motion

By a motion dated 11 February 1992, the CPA requested that the Secretary of the Board issue a subpoena requiring certain employees of PG&E and PGT to appear as witnesses in this hearing, that the Board order that those witnesses be examined *ex juris*, in the State of California, before a Commissioner appointed by the Board, and that the Board issue a letter of request to the United States District Court for the Northern District of California to cause those witnesses to appear before the Commissioner to be examined in respect of the changed circumstances and new facts that have arisen since the GH-5-88 Decision.

By a subsequent letter dated 20 February 1992, the CPA amended its motion to include requests that the Board issue a subpoena requiring that a representative of the CPUC appear, as well as a witness in this proceeding to speak to the letter of comment which the Commission had filed with the Board on 11 February 1992 or, in the alternative, that the Board direct that the CPUC letter of comment be struck from the record in this proceeding.

The CPA motion followed an earlier request to the Board by the CPA to require that A&S, ANG, PG&E, and PGT, all of which had intervened in this proceeding, should be directed to file written evidence and produce witnesses to be cross-examined at the hearing. The CPA also requested that the Board invite the CPUC to participate in the hearing.

In response to this request, the Board advised A&S and ANG, by letters dated 23 January 1992, that it expected both companies to file written evidence and have witnesses available for cross-examination at the hearing to address the issues raised in this proceeding. The Board also indicated that both A&S and ANG could choose to produce witnesses from affiliated companies or have such affiliated companies, presumably PG&E and PGT, support them in the presentation of their evidence by participating in the hearing. In addition, by letter dated 23 January 1992 addressed to the Executive Director of the CPUC, the Board indicated that there were no obstacles to the participation of the Commission in the oral portion of the hearing; however, the Board advised that any witness appealing for the CPUC should be a person with full and unequivocal authority to address the policies,

objectives and decisions of the Commission affecting Canadian gas sales to California. The Board was informed that the CPUC intended only to comment on the merits of the CPA application.

By letters of 3 February 1992 from their Canadian counsel, both PG&E and PGT informed the Board that they could not offer written evidence and provide witnesses in this proceeding without the risk of severe prejudice to their legitimate interests in court actions brought against them in Alberta for alleged contract breaches and wrongful interference with the contractual relationship between A&S and its producers. PG&E also indicated that it is the subject of a CPUC review into the reasonableness of its Canadian gas purchases for the years 1988 through 1990. Both A&S and ANG complied with the Board's direction and filed written evidence and undertook to produce witnesses to address their evidence in this proceeding.

The CPA motion, as amended, was argued on 24, 25 and 26 February 1992 as a preliminary matter at the commencement of this hearing.

Counsel for the CPA submitted that the GH-R-1-91 proceeding was not a hearing into an application for a licence or certificate where the Board's practice is that the applicant should be permitted to frame its own case and present its evidence in the manner that it chose. Rather, the CPA argued that this proceeding was both a review and an inquiry into the changed circumstances and new facts that have arisen since the GH-5-88 Decision and that, accordingly, it was up to the Board to determine what evidence was required and to cause parties to present this evidence to the Board. The CPA argued that the Board risked having virtually no record upon which a decision could be made or that it would not have the best evidence upon which to decide the case before it. In this regard, the CPA argued that the witnesses from PG&E and PGT, who testified before the Board in the GH-5-88 hearing and who were familiar with the California market issues as well as the policy matters of A&S, PG&E and PGT, were essential to this proceeding. Moreover, the CPA argued that the Board has the power under section 11 of the NEB Act, under the draft NEB Rules and under common law to compel the attendance of PG&E and PGT witnesses before a Commissioner to be examined in California on the issues of this proceeding.

The CPA submitted that under section 11 of the Act the Board has the powers of a superior court of record to summon and compel the attendance of witnesses, to conduct the examination of witnesses, and to enforce its decisions and orders. Furthermore, the Board has the power to issue subpoenas as provided for in Rule 20 of the draft NEB Rules and by Rule 36(3) to take evidence on commission.

Furthermore, the CPA held that the Board could make a request for the assistance of a court in another jurisdiction and that the Board could issue, in aid of its commission to take evidence outside its jurisdiction, a letter of request or letters rogatory addressed to a foreign court. The CPA submitted that a superior court of record has an inherent jurisdiction to issue letters rogatory and it proposed that such a letter be issued to the District Court of the District of Northern California requesting that Court to allow the Board, as a commission, to take the evidence in accordance with the draft NEB Rules of the Board and with cross-examination to be conducted by Canadian counsel. The CPA further submitted that there was reasonable probability of a letter being effective and, in support of this assertion, it cited section 1782 of Title 28 of the United States Code Service which, it held, empowers the District Court to give effect to a letter rogatory issued by a foreign tribunal such as the Board.

With respect to the CPUC letter of comment, the CPA argued that it constituted evidence which should be subject to cross-examination since it made assertions of fact and opinion which were clearly

contrary to the evidence on the record and that it expressed strong adversarial positions on fundamental issues in this hearing. The CPA was of the view that it was a denial of natural justice to refuse to allow cross examination on the CPUC statements contained in the letter of comment and that, accordingly, the Board should also proceed by way of subpoena, commission and letters rogatory to compel the CPUC witness to speak to its evidence. In the alternative, the CPA urged the Board to strike the CPUC letter of comment from the record of this proceeding.

IPAC, the Ministry of Energy, Mines and Petroleum Resources of British Columbia and the Ministry of the Attorney General for the Province of British Columbia ("B.C."), and the APMC supported with some reservations the motion of the CPA, as amended. IPAC did not think it was appropriate to take steps to compel the CPUC to present a witness in this proceeding but rather preferred to have the CPUC letter of comment struck from the record. B.C. likewise did not think the Board should exercise its power to compel evidence from the CPUC. The Province did, however, agree with the position of the CPA on the question of the evidence to be sought from the PG&E and PGT officers and employees and on striking the CPUC letter of comment from the record. The APMC spoke only to the treatment of the CPUC letter of comment and supported the view that it should be struck from the record.

Brymore Energy Limited ("Brymore"), the CPUC, PG&E and PGT spoke in opposition to the CPA motion. Neither PG&E, PGT nor Brymore addressed the CPA amendment pertaining to the CPUC letter of comment while counsel for the CPUC, for his part, dealt only with the question of the validity of the letter of comment.

PG&E reiterated its reasons for not filing evidence or producing witnesses on the grounds that it would be exposing itself to unfair risks because of its involvement in court actions brought in Alberta by several gas producers alleging that A&S breached contracts with them; that PG&E induced A&S to commit the alleged breaches; that PG&E otherwise interfered with the contractual relationship between A&S and its producers; and that PG&E is responsible for A&S' debts. The plaintiffs in those court actions are Amoco Canada Petroleum Company Ltd. and Amoco Canada Resources Limited, Shell Canada Limited and Chevron Canada Resources. PG&E pointed out that all are members of the CPA and each one is an intervenor in this proceedings. PG&E also explained that it is engaged in confidential commercial negotiations with A&S' producers to restructure its gas supply arrangements from Alberta and British Columbia. Finally, PG&E stated that it is the subject of a formal review now being conducted by the CPUC into the reasonableness of its Canadian gas purchases for the years 1988 through 1990 and that, for these reasons, it feared that its participation in this hearing could become a form of pretrial discovery for the Alberta court actions, an effort to force disclosure of confidential and sensitive commercial negotiation strategies and the results of a premature examination on the issues pertaining to the CPUC's Reasonableness Review.

PG&E further argued that nothing the CPA is seeking by its application for review of the GH-5-88 Decision requires the evidence of PG&E. It contended that the CPUC decisions are a matter of public record and that the changed circumstances and new facts in the California market flow from those decisions. Moreover, PG&E was of the view that the Board did not possess the necessary powers to grant the relief sought by the CPA and that, while the Board has the discretionary power to issue the requested subpoena, it would only be effective in Canada and it would thus constitute a nugatory action to compel the attendance of California witnesses.

PG&E contended that, while the Board has, by virtue of section 11 of its Act, all such powers, rights and privileges as are vested in a superior court of record with respect to the attendance, swearing and examination of witnesses, it is nevertheless not a superior court of record and does not have any inherent jurisdiction. Rather, the Board derives its powers from the NEB Act and its Regulations and it is therefore questionable whether the Board has jurisdiction to issue letters rogatory to give effect to commissions conducted outside the country. Indeed, PG&E questioned whether a court in California would execute on letters rogatory issued by the Board and argued that the CPA had not appropriately established the content and meaning of the law of California and for these reasons had failed to establish a reasonable probability that an order of the Board would be effective. Consequently, PG&E urged the Board to deny the CPA motion.

PGT adopted the arguments of PG&E concerning subpoenas and letters rogatory and reiterated the position it had expressed in its letter of 3 February 1992 to the Board. It submitted that the court actions went to the very heart of the matters on which the CPA sought to obtain evidence. PGT also submitted that the CPA had failed to demonstrate that the interest of the Canadian public would suffer in the absence of witnesses from PGT and PG&E.

Brymore questioned the CPA's interest in seeking a review of the GH-5-88 Decision. According to Brymore, the CPA had repeatedly represented that it was not a party to any of the contracts involving A&S, PG&E and PGT and yet it was seeking orders from the Board which would have an impact on the negotiations to restructure those contractual arrangements. Brymore was of the view that the policy of the Board to let the applicant make its own case should prevail and that the CPA should not be permitted to shift to others this onus to prove its case. By its application for review, the CPA was not looking for any changes to Licences GL-99 or GL-111. On the contrary, it wanted them upheld and strengthened and, in those circumstances, there was no need for evidence from PG&E or PGT. It was Brymore's view that the best evidence as to the policies of the CPUC ought to come from the CPUC, not from PG&E and PGT.

Counsel for the CPUC submitted that the Commission's submission of 11 February 1992 was a valid letter of comment and that by so doing the CPUC had foregone its rights to submit evidence, to cross-examine other parties, to submit argument and to be served with the documents in the proceedings. Counsel for the CPUC acknowledged that the CPUC was aware that a letter of comment carries less weight than evidence since it is untested by cross-examination. Counsel for the CPUC argued that there were no preconditions in the draft NEB Rules which precluded the CPUC from filing such a letter of comment and that the CPUC would find it unfair if its letter of comment should be struck from the record simply because the CPA does not agree with the views expressed therein. Moreover, the NEB Rules provide a recourse to deal with a letter of comment when a party disagrees with its contents. Rule 33(4) provides the CPA with an opportunity to file a reply on the CPUC and to file a copy of that reply on the Board and every party to the proceeding within fifteen days of receipt of the letter of comment.

Views of the Board

The Board issued its ruling on the CPA motion at the GH-R-1-91 proceeding on 4 March 1992 and it is reproduced below in its entirety:

The Board has carefully considered the submissions of the parties and has reviewed the various authorities which have been cited to it during argument. The Board has

also considered the record of the GH-5-88 proceeding and has researched further authorities on the legal arguments presented to it by the parties.

The question of whether to compel PG&E and PGT witnesses to appear will be addressed first and the amendment to the CPA motion with respect to the CPUC letter of comment will be dealt with afterwards.

Firstly, the Board agrees with those parties who have recognized that the issuance of subpoenas and the taking of commission evidence by the Board are matters subject to its discretion. This is so whether the Board is a superior court of record or simply a court of record and whether it would have inherent jurisdiction or not. The Board is, however, of the view that it has, for the purpose of those matters listed in subsection 11(3) of its Act, all such powers, rights and privileges as are vested in a superior court of record including the right to take commission evidence if necessary and appropriate in its discretion. It is the power to issue letters rogatory or letters of request that has generated the strongest arguments among the parties and the Board recognizes that the question is of great consequence.

The issuance of letters rogatory is an extraordinary recourse not often used by tribunals and is only resorted to in very exceptional circumstances as was well-established by the case law presented to the Board by the various parties. Letters rogatory are matters of international law based on the principle of comity of nations and are given effect in the foreign jurisdiction not as a matter of legal obligation but out of mutual deference and respect. Their purpose is to seek in foreign countries evidence which is necessary for the purposes of justice in the domestic courts. However, their effectiveness in the foreign jurisdiction is often uncertain, their form is not well established, and their issuance appears to be dependent upon the inherent powers of the tribunal wishing to use such recourse.

In this case, the Board's jurisdiction to issue letter rogatory has been seriously questioned by parties and the doubt that has been raised about the powers of the Board in this regard persists. The Board recognizes that it is not a court of inherent jurisdiction but, as previously held, it considers itself vested with the powers of a superior court of record for the purposes of attendance, swearing and examination of witnesses. While the Board has not concluded that it lacks authority to issue letters rogatory, it questions the appropriateness of resorting to such an extraordinary procedure in the context of this proceeding and for the purposes sought by the CPA.

The Board is far from convinced that a letter rogatory seeking the assistance of the California courts for the examination of witnesses' views on the advisability of reviewing a regulatory decision would automatically be given effect in the foreign jurisdiction. The Board is also uncertain as to the amount of Time that it would take to have any such request enforced in California and to receive the evidence that the CPA is seeking. The Board believes that final decisions with respect to GH-R-1-91 must be made in a timely fashion and prolonging the proceeding risks unduly affecting the rights of some parties.

More importantly, the Board has not been persuaded that the evidence that the CPA wishes to present through witnesses from PG&E and PGT is necessary to this proceeding. Parties have recognized, and the Board concurs, that there is discretion to be exercised by the Board in deciding to issue subpoenas and in obtaining commission evidence. The Board is of the view that this same discretion exists in deciding to issue letters rogatory.

The Board, while recognizing that this proceeding is both a review of GH-5-88 and an inquiry into the effects in Canada of recent CPUC actions, does not agree with the CPA that it necessarily has to hear from the PG&E and PGT witnesses because they were parties in the original GH-5-88 proceeding or because their views are essential to the Board's inquiry. Exercising its discretion, the Board had already determined and indicated in its letter of 23 January 1992 to the CPA that it did not intend to direct PG&E and PGT to file evidence or to provide witnesses at this proceeding. The Board, however, upholding the principle that an applicant should be permitted to frame its case and present its evidence in the manner that it chooses, considered the CPA motion as a request to compel the attendance of witnesses whose examination the CPA considered necessary for it to make its case before the Board.

Having heard the CPA arguments and those of the parties who supported and who opposed the CPA request, the Board is not persuaded that the evidence that is sought to be presented by the examination of the PG&E and PGT witnesses is essential to convince the Board that it should do what it has been petitioned to do by the CPA in its application for review. Neither is the Board persuaded that the potential value of such evidence would be sufficient to justify the very unusual step for a tribunal such as the Board to issue letters rogatory. Furthermore, the Board is not persuaded that evidence which might be available from PG&E and PGT could be obtained or would likely be available in a timely manner to be of use in this proceeding, given the uncertainties and probable delays in related American court processes.

The Board considers that much valuable evidence as to the issues the Board is inquiring into has already been put on the record of this proceeding, largely by the efforts of the CPA drawing on the voluminous material which is already in the public domain as a result of regulatory activities in California. As well, the entire record of the GH-5-88 proceeding has been incorporated into the record of this proceeding.

While the Board wishes to ascertain the new facts and changed circumstances which have arisen since its original decision, the views of various parties on those changes are not, in the Board's view, essential to any determination that it may have to make. It does not appear necessary to the Board to rehear the evidence which was adduced at the original GH-5-88 proceeding. Neither is it necessary to rehear each party which participated in the original proceeding in order to review the decision in light of changed circumstances or new facts otherwise established before the Board. The Board is of the view that whatever elements of the Canadian public interest may have been affected by recent CPUC actions can be effectively reviewed by the Board without receiving the views and opinions of PG&E and PGT on those regulatory actions.

The Board has, therefore, determined that the evidence of witnesses from PG&E and PGT which the CPA seeks to obtain by the issuance of subpoenas, commissions and letters rogatory is not necessary to the Board to review its GH-5-88 Decision and to fully inquire into the issues set out in the GH-R-1-91 Hearing Order and the Board therefore denies that portion of the CPA motion of 11 February 1992, as subsequently amended.

With respect to the CPA request to strike from the record the CPUC letter of comment of 11 February 1992, the Board was persuaded by the arguments of counsel for the CPUC. Although parties may strongly oppose the views expressed therein, although the CPA may wish to cross-examine a witness from the CPUC and although the authority of the writer of the letter may not be clearly established, the CPUC submission does constitute a letter of comment within the meaning of the Board's *Rules of Practice and Procedure* which should be allowed to stay on the record in this case. The CPUC has not intervened in the proceeding and will enjoy none of the rights and privileges granted to intervenors. The views and opinions expressed in the letter of comment will surely be addressed by those opposed to them in their respective final arguments. The weight that the Board will give to the CPUC letter of comment will not be what it might have given to tested evidence and the CPUC is aware of that and accepts it. Having regard to the very nature of a letter of comment and its probative value in the Board's process, the Board cannot agree with the CPA that to leave it on the record without subjecting the writer to cross-examination amounts to a denial of natural justice. A letter of comment is not evidence; it does not carry the weight of evidence, it can be contradicted by evidence and attacked in argument. The CPA's rights seem to be well enough protected.

The CPA motion is therefore denied.

The above decisions and reasons, therefore, constitute the Board's ruling on the CPA motion of 11 February 1992, as amended on 20 February 1992, and it has been requested by the Board that it be reproduced in the transcript of the proceedings to become part of the record.

3.3 Issues Addressed in the GH-R-1-91 Proceeding

3.3.1 Issues a) and b):

the effects of the regulatory actions and decisions taken in California on existing and proposed exports of Canadian gas authorized by the Board under Licences GL-99 and GL-111; and

the consequences of these actions and decisions on the Board's findings and decision in GH-5-88 which were rendered under the Board's Market-Based Procedure.

3.3.1.1 Views of the CPA

The CPA took the position that the CPUC's SPURR Decision, the Capacity Brokering Decision and Resolution G-2967, among other regulatory actions and decisions, would significantly reduce A&S' sales because these decisions ordered PG&E to give up its capacity on PGT which it needs to transport A&S' gas to PG&E's market. The CPA believed that these CPUC actions and decisions would have a severe and detrimental effect on the gas exports authorized by the A&S Licences.

The CPA argued that the implementation of Resolution G-2967, which initially provides for the conversion of 30 MMcfd from sales rights to transportation rights, would result in the displacement of PG&E's purchases from PGT, and consequently from A&S, by other Canadian gas supplies to serve the SPURR Project and that the evidence indicated that some capacity on PGT had already been converted to serve the SPURR Project. During cross-examination, the CPA witnesses stated that the SPURR Decision could reduce A&S' sales by as much as 10 percent (100 MMcfd). Thus, they argued the SPURR Decision "undermines the export and import approvals granted by Canadian and United States governmental bodies, abrogates the contractual obligations of PG&E to Canadian producers and runs counter to the intent of the Access Agreement".

With regard to the Capacity Brokering Decision, which contemplates the full conversion of PG&E's purchase of sales service on PGT to transportation service, the CPA submitted that, in a worst-case scenario, 100 percent of A&S' volumes could be displaced. The CPA stated that, at the GH-5-88 proceeding, PG&E had said that all space on PGT was dedicated to move A&S' gas to the Northern California market. Consequently, the Decision could potentially abrogate the gas sales contracts between PGT, A&S and its producers as well as the PGT transportation arrangements. The CPA therefore argued that the Capacity Brokering Decision denies the existence of obligations on the part of PG&E to purchase gas from any Canadian producer or A&S producers and does not address transition costs.

With regard to the transition costs, the CPA noted that the Decision states that if there were PG&E liability and damages, there was no record on the issue of whether such damages were solely the result of CPUC regulation and not the result of the operation of economic forces in the market. Thus, the CPA concluded that the CPUC was not prepared to recognize that it was its regulatory action which was forcing the restructuring of the contracts. It was, as well, CPA's view that the CPUC's Reasonableness Review of PG&E's purchase of Canadian gas would bias private contract renegotiations because the Commission was not only going to look back at how PG&E operated its gas procurement practices but was also going to look prospectively at how the restructuring would be undertaken.

The CPA also noted that the evidence in the GH-5-88 proceeding was that A&S' gas would serve not only the core market but all markets served by PG&E. During cross-examination, the CPA established that the forecast of requirements for Canadian gas prepared by PG&E for the GH-5-88 proceeding included the UEG market and that this particular market had been prohibited by the CPUC, in its Gas Procurement and Transportation Decision, from purchasing 35 percent of its gas requirements from PG&E's system supply. Furthermore, as a result of the Capacity Brokering Decision, the UEG Department of PG&E would no longer be able to purchase any gas from PG&E's system supply within five years. The Association estimated a potential loss of 350 MMcfd of sales to the A&S producers stemming from these decisions.

The CPA also argued that the degree to which currently contracted Canadian supplies would be affected by the CPUC regulatory decisions was illustrated in PG&E's brochure "Looking at the Future", filed at the hearing by A&S as Exhibit C-1-6. It showed that, in PG&E's view, it could potentially reduce its demand for A&S contracted gas from the 1.1 Bcfd that existed when A&S entered into the long-term contract that supported the GH-5-88 Decision, to 650 MMcfd by August 1992, and to about 550 MMcfd by 1996, when CPUC's new rules are fully implemented.

The CPA argued that, in the GH-5-88 Decision, the Board used its Market-Based Procedure to comply with the requirements of Section 118 of the Act and that, with respect to the consideration of other factors under the MBP in its determination of the public interest, the Board specifically included gas supply, transportation arrangements and markets. With respect to the MBP, the CPA referred to the Board's GHR-1-87 Decision which indicated that it would consider evidence that the export volumes would be taken and evidence about the availability of pipeline space. The CPA also stated that the MBP requires the Board to take into account information on any relevant government policies or positions. More specifically, the GHR-1-87 Decision stated that Canadian energy policy is the premise which forms the basis of the MBP and that policy, in turn, is based on the premise that the marketplace should determine the supply, demand and price for natural gas. Therefore, the CPA argued that these factors should be determined by the marketplace, not by regulators.

It was CPA's view that the CPUC's actions are contrary to the principles of deregulated markets and prices and to the principle of contract sanctity that underlies these principles. Moreover, the CPUC's actions are contrary to the representations made by the CPUC in the GH-5-88 proceeding, wherein it filed a letter supporting the extension of Licence GL-99 and referred to A&S' gas supply to PG&E as part of a "gas supply portfolio which is very competitive under the market-driven regulatory framework the CPUC has encouraged".

The CPA argued that, notwithstanding the support the CPUC expressed for the PG&E/PGT/A&S contractual arrangements in the GH-5-88 proceeding, the CPUC, in its Contract Renegotiation Decision, directed PG&E to renegotiate the A&S contracts which underpinned gas supply in the GH-5-88 proceeding. This CPUC Decision, according to CPA, would "raise the spectre of a policy that required the price of gas to be determined at the wellhead, not the burner-tip, as was contemplated by the netback contracts and the government approvals". Moreover, the CPA pointed out that the A&S producers had given up 90 percent take-or-pay contracts to get market-oriented pricing that ensured that gas would always be taken to meet the market and to get an equitable take provision. Together, these two things would ensure that, in the marketplace, the A&S gas would always be competitive with alternate supply.

In addition, the CPA argued that Canadian producers undertook large investments to develop additional supplies based on their contractual commitments to PG&E through A&S and on the representations made by A&S, PGT, PG&E, the CEC and the CPUC during the GH-5-88 proceeding. These latter representations confirmed the expectation of high takes of A&S' gas under the PG&E/PGT/A&S contractual arrangements and established the need for development contracts.

Therefore, the CPA concluded that the present actions of the CPUC undercut the contracts which its former actions had inspired and, more importantly, the CPUC's regulatory actions "effectively direct abrogation of the freely negotiated contractual undertakings upon which the GH-5-88 Decision was based". Moreover, those actions implied that "regulators in gas-consuming jurisdictions will completely

control international gas trade". In particular, the CPUC is purporting to extend its jurisdiction into Canada by directing the renegotiation of contracts between A&S and its Canadian producers and directing PG&E to convert its capacity on PGT which is regulated by the FERC.

3.3.1.2 Views of Interested Parties

IPAC, APMC, B.C. and Pan-Alberta Gas Ltd. ("Pan-Alberta") supported the CPA position that the CPUC's actions and decisions would have a significant negative impact on the volumes of gas flowing under A&S Licences GL-99 and GL-111.

These parties argued that the CPUC decisions and actions were inconsistent with the evidence presented in the GH-5-88 proceeding and with the representations made by parties in that proceeding. It was their view that the CPUC decisions would undermine the freely-negotiated contracts which the Board had found to be in the public interest in applying its MBP. IPAC also argued that the CPUC had ignored Canadian jurisdictions, including that of the Board, with respect to Canadian transportation and export approvals.

IPAC, APMC and B.C. also took the position that Canadian gas producers had undertaken major capital investments to develop additional gas supplies to serve PG&E's market on the strength of the representations made in the GH-5-88 proceeding. B.C. estimated that such investments made by the producers in its province could be as much as one billion dollars. The province argued that the CPUC actions could have the effect of stranding those investments. One producer, Conwest Exploration Company Limited ("Conwest"), stated that it had spent 40 million dollars to explore for and develop 100 Bcf of gas reserves to meet its future supply commitments to A&S.

PG&E and A&S generally agreed that the effect of the CPUC's actions would be a reduction in the market which PG&E could serve and therefore would significantly reduce the amount of gas required from A&S. It was their view that the overall demand for Canadian gas in Northern California would not decline and that only the manner in which Canadian gas would be sold and exported to California in the future would change. Therefore, these companies argued that the quantification of the impact of the CPUC's actions at this time is somewhat speculative. PG&E argued that the Board's finding in the GH-5-88 Decision that the Northern California market is proven and highly dependable was correct then and is still true now, and agreed that the Capacity Brokering Decision, if implemented, would significantly change the requirements for A&S' gas. PG&E further noted that the Capacity Brokering Decision, which applies to all utilities in California, may never be implemented in its current form. It was PG&E's view that Canadian producers entered into contractual arrangements knowing that the PG&E market would be subject to the gas purchasing policies of the CPUC.

During cross-examination, A&S' witnesses confirmed that the PG&E conversion of some sales to firm transportation on PGT, as ordered in Resolution G-2967, was effective 1 February 1992 and that 300 Mcfd of gas was currently flowing on PGT under the SPURR Project. A&S also confirmed that this Resolution would reduce the amount of capacity available on PGT to transport A&S sourced gas. In addition, A&S confirmed that, at the time of the GH-5-88 proceeding, PG&E's Canadian gas requirements for its UEG market were met entirely by A&S supplies. As a result of the CPUC decisions on UEG gas supply arrangements, the proportion of PG&E's UEG requirements which can be met from PG&E's system supply (which includes A&S' gas) will be progressively curtailed even if the price is competitive. Thus, A&S noted that the full volumes of Licences GL-99 and GL-111 may not be required for the entire period unless A&S can find other markets within California apart from

PG&E. As to the Capacity Brokering Decision, A&S' witnesses stated during cross-examination that PG&E was directed to implement the decision regardless of any contractual arrangements entered into by PG&E through its subsidiaries, PGT and A&S.

3.3.1.3 Views of the Board

The Board is persuaded by the evidence that the recent CPUC actions and decisions relating to PG&E's gas purchase and transportation arrangements will have the effect of substantially reducing A&S' export sales under Licences GL-99 and GL-111. In the Board's view, it is possible that, by 1996, PG&E's demand for PGT's sales gas from A&S, and consequently from A&S producers, could be reduced by as much as 50 percent, that is to 550 MMcfd from 1.1 Bcfd.

This contrasts with the evidence in the GH-5-88 proceeding that rates of take from A&S' supply close to 100 percent would continue because of the competitive terms of the international contract. This expectation of a high load factor was created by the submissions made by interested parties, including the CPUC, that A&S' gas, which constituted a competitive and secure long-term supply, was needed in a durable and growing market. The Board notes that the evidence in the current proceeding is that a substantial proportion of A&S' gas may not be taken even if it is priced to compete with supplies of U.S. gas in the California market. This is, in the Board's view, contrary to the evidence adduced at the GH-5-88 proceeding.

The international contract, and the related A&S producer contracts, underpin the long-term licence authorization which resulted from the GH-5-88 proceeding. The evidence in that proceeding, which the Board relied upon, was that the international contract between A&S and PGT provided flexible and competitive terms which included an equitable take provision by PG&E from A&S, provided the price in the market area served remained competitive. The Board believes that the CPUC decisions and not market forces will affect the manner and the extent to which gas will flow under these contracts which were negotiated in good faith. Moreover, because responsibility for approval of the terms of these contracts resides with jurisdictions other than the CPUC'S, including that of the Board, the effect of the CPUC decisions is to extend its jurisdiction beyond the boundaries of the State of California.

In the GH-5-88 proceeding, A&S proposed to rely increasingly and preponderantly on development contracts as a means of providing the California market with a secure long-term supply of gas. At the time of that proceeding, evidence that gas would continue to be sold to Northern California via the A&S, PGT and PG&E contractual chain gave producers the confidence to invest in the development of new supplies for that market. The effect of recent CPUC decisions is to restrict the entry of these gas supplies to the market for which they were developed on the terms and conditions under which those investments were made. The Board concludes that the CPUC decisions could strand substantial producer investments. At the very least, the Board finds that these decisions undermine the contractual basis on which the investments were made and adversely affect their prospective economic viability.

In the Board's view, therefore, the evidentiary underpinnings of its GH-5-88 Decision have been substantially changed and the Canadian public interest, which it found to be served by the issuance of Licences GL-99 and GL-111, has been adversely affected.

The Board concludes that it cannot condone or ignore the impact of regulatory actions taken by other jurisdictions which fundamentally change the basis upon which it was persuaded to issue a licence and which impose changes within its jurisdiction.

3.3.2 Issue c):

the likelihood of commercial restructuring of the long-term contractual arrangements underpinning the export licences in view of these actions and decisions and the appropriate period of time for it to take place.

3.3.2.1 Views of the CPA

The CPA stated that no parties quarrelled with the need for commercial restructuring but there was a debate on what was needed to allow restructuring to happen and what was the probable timing. The Association stated that the three-year transition period contemplated in the Access Agreement, which the CPUC had "applauded", was more reasonable than what the CPUC proposed. The CPA noted that the renegotiations involved a large number of contracts and producers and argued that more time was needed than permitted in the Capacity Brokering Decision. The CPA argued that the relief it sought from the Board was required to create a regulatory balance to facilitate fair negotiations. In its view, no deadline should be imposed on the restructuring negotiations because this would unfairly place Canadian producers at a disadvantage.

It was the CPA's view that any transition costs relating to restructuring of Canadian supply arrangements should be dealt with in the commercial renegotiations. In light of the DRA claim in the Reasonableness Review, it would be very difficult for PG&E to negotiate in good faith in the absence of some guidance from the CPUC on the treatment of transition costs. The actions of the CPUC, including the Reasonableness Review Proceeding and the Capacity Brokering Decision, operate to bias the commercial negotiations. Furthermore, the CPA argued that PG&E has taken the position before the CPUC that any transition costs and any costs relating to restructuring of Canadian supply arrangements should be dealt with by the CPUC and that they should be able to be passed on.

3.3.2.2 Views of Interested Parties

There was general agreement among interested parties that commercial arrangements need to be restructured to reflect the altered California marketplace. However, there were differences among them as to the time required to accomplish the restructuring.

IPAC, B.C. and APMC, which advocated that the Board take measures to counteract the CPUC's regulatory actions, also indicated that more time would be required than was contemplated by the CPUC's Capacity Brokering Decision. These parties also argued that transition costs must be addressed in the renegotiation process.

Furthermore, IPAC, B.C., APMC and Pan-Alberta submitted that a countervailing regulatory action was required to facilitate this renegotiation process. In particular, IPAC stated that there were factors which complicated the negotiations. For example, A&S has some 600 supply contracts with over 190 producers. All of these producers would have a commercial interest in the restructuring because the sales between A&S and PG&E are not arm's-length. A further complication was that the transportation rights currently facilitating the sales arrangements fall within the jurisdiction of three regulators. The FERC regulates PGT; the Board regulates ANG; and NOVA is regulated within Alberta. Furthermore, any amendments to the A&S export/import authorizations would require the approval of the Board and the U.S. DOE. IPAC stated that, even with good faith among the parties involved, the process of

restructuring would be lengthy. In IPAC's view, the most critical issue with respect to restructuring was to create a fair, balanced environment for it to take place.

Although they did not question the jurisdiction of the CPUC to restructure the California gas market, IPAC, APMC and B.C. argued that, in advance of pursuing any major restructuring which would affect existing contractual arrangements, the CPUC should allow for and encourage good faith commercial negotiations to restructure existing arrangements so as to be responsive to the changes the Commission seeks.

On the other hand, A&S was of the view that negotiations under the auspices of the Energy Consultative Mechanism were well under way and hoped that an agreement in principle would be reached in the summer of 1992. Poco Petroleums Ltd. ("Poco") supported A&S' views and noted that the 1985 Agreement on Natural Gas Markets and Prices contemplated a transition period of only one year.

PG&E pointed out that the costs associated with the restructuring of Canadian supplies would be examined by the CPUC at a subsequent Reasonableness Review as indicated in the Capacity Brokering Decision. It argued that, without a deadline, the restructuring would drag on; consequently the sooner it took place, the better it would be for everyone because of the certainty the completion of restructuring would provide.

3.3.2.3 Views of the Board

The effect of the CPUC Capacity Brokering Decision is to shorten considerably the three-year transition period contemplated by parties to the Access Agreement which the CPUC had previously "applauded" in its Gas Procurement and Transportation Decision in September 1990. The CPUC Capacity Brokering Decision of November 1991 would see the transition period end as early as October 1992. In the Board's view, the evidence indicates that the complexity of the contractual arrangements among a large number of parties warrants the provision of more time for an orderly transition and for all parties to seek fair and equitable settlements in good faith through private contractual negotiations.

Moreover, the Board agrees with those parties who argued that the CPUC's actions tend to create a bias against Canadian interests in the process of restructuring existing contractual arrangements. This occurs because the Commission has given PG&E no indication whether it will be able to pass on to its ratepayers any costs it may incur as a result of restructuring supply arrangements with Canadian producers.

For these reasons, the Board is unable to reach any conclusion as to the likelihood or timing of commercial restructuring of long-term contractual arrangements underpinning A&S export licences.

The Board also notes that, upon completion of the commercial restructuring, any amendments to export authorizations, sales contracts and transportation arrangements under this Board's jurisdiction will have to be filed for review and approval by the Board.

3.3.3 Issue d):

> Whether it is permissible within the Board's current authority and, if so, whether it is desirable for the Board to attach a condition to all short-term export orders that would prohibit exports at Kingsgate, British Columbia, of any Canadian gas destined for utilization in the Northern California market that is not gas presently contracted by A&S for sale to PGT and, if so, for what period of time should such a condition remain in effect.

At the conclusion of the evidentiary portion of the GH-R-1-91 hearing, the Board requested Counsel, in addressing Issue d) in argument, to consider the Board's Act, its regulations and any other legislation, including the Free Trade Agreement, which bears on the aspect of permissibility.

3.3.3.1 Views of the CPA

The CPA expressed its views on Issue d) in its submissions to the Board in respect of the interim measures, in its written evidence and, more extensively, in its final argument.

The CPA took the position that the Board had the authority to condition all short-term export orders as the Association had requested and that it should do so until restructuring of existing long-term contracts was completed and all Canadian and United States regulatory tribunals have, after due process, granted all approvals necessary to allow the restructured contracts to govern.

It was the CPA's view that the powers granted to the Board under sections 21 and 19 of the NEB Act clearly permit the implementation of the requested condition. Subsection 21(1) of the Act allows the Board to "review, vary or rescind any decision or order made by it" and, relying on the Board's *Reasons for Decision In the Matter of An Application by Cyanamid Canada Pipeline Inc. Pursuant to Section 12(1) of the Act for Review of the jurisdiction contained in the National Energy Board Reasons for Decision in the Matter of an Application Under Section 49 and Subsection 59(3) of the National Energy Board Act* of Cyanamid Canada Pipeline Inc., December 1986 GH-3-86 ("GH-3-86 Review") the CPA argued that the discretion of the Board to review and vary any order is unfettered.

For the CPA, section 19 of the NEB Act allows the Board to make interim orders and to condition any orders. Subsection 19(1) of the NEB Act was quoted by the CPA as the authority for the Board to condition the short-term export orders as proposed by the CPA and to make such a condition to have force until the happening of a specific event, such as the completion of restructuring and approval of the new contracts by all regulatory tribunals.

While the CPA recognized that the Governor in Council is empowered by paragraph 119.01(f) of the NEB Act to make regulations respecting the conditions that the Board may include in orders, it was of the opinion that such conditions are not limited to those set forth in subsection 8(3) of the *National Energy Board Part VI Regulations* ("Part VI Regulations"). The CPA submitted that the power to make regulations is permissive, not exclusive, and is subject to the general conditioning power of the Board under subsection 19(1) of the NEB Act.

The CPA further submitted that any breach of the requested condition, such condition having been imposed under the authority of Part VI, Division III of the NEB Act and the Part VI Regulations, would be a contravention of the NEB Act and the regulations made under it within the meaning of

subsection 121(l) of the Act and would constitute an offence for which the Board could seek a fine on conviction.

The CPA also took the position that the Free Trade Agreement does not act as a bar to the implementation of conditions on short-term orders.

Looking first at the NEB Act, the CPA pointed to section 119.2 of that Act which requires the Board to give effect to the FTA in exercising its powers. The CPA also referred to subsection 119.5(l) of the Act which requires that the Board not refuse to issue, revoke, suspend or vary a licence or order for the exportation of energy goods to the United States, if to do so would constitute the maintenance or introduction of a restriction on exportation as a consequence of which any of subparagraphs (a), (b) or (c) of Article 904 of the FTA would apply. The CPA admitted that the Board must give effect to the FTA and must also have regard to the proscription contained in subsection 119.5(l) of the NEB Act, if it is to impose a restriction on the export of any energy good.

The CPA further argued, however, that a "restriction" for the purposes of the FTA is, as defined in Article 901 of the Agreement, "...any limitation, whether made effective through quotas, licences, permits, minimum price requirements or any other means;". Pointing to Article 902.1 of the FTA, in which Canada and the United States affirm their respective rights and obligations under the *General Agreement on Tariffs and Trade* ("GATT") and to Article 902.2, where those parties clarify their understanding that minimum export price requirements are also prohibited under GATT, the CPA submitted that the condition which is requested to be attached to short-term export orders is neither a minimum price requirement nor a quantitative restriction on the total volume of gas exported from Canada.

The CPA also argued that even if the requested condition did constitute a restriction, it is not one which is prohibited under subsection 119.5(l) of the NEB Act. Subparagraphs (a), (b) or (c) of Article 904 of the FTA would not apply. Because there would be no reduction in the volume of gas available for export to the United States, the proportionality condition of subparagraph 904(a) would continue to be maintained. No minimum export price is set by the imposition of the requested condition and the requirement of subparagraph 904(b) that a party not impose a higher price for exports of an energy good than the price charged for such energy good when consumed domestically will not be breached. Finally, the CPA argued that, for the same reasons that the proportionality test will not be invoked by the imposition of the condition, there will be no disruption of normal channels of supply to the United States or normal proportions among the specific energy goods supplied to the United States. In these circumstances, subparagraph 904(c) of the FTA will not be breached either.

The CPA was also of the view that the spirit of free trade also involves the concept of minimization of regulatory interference with contracts and argued that implementation of conditions on short-term export orders would enhance such a spirit of free trade, because it would give a clear indication that the Board is supportive of the free trade concept that freely-negotiated contracts should govern, free of regulatory interference.

With respect to the desirability of the requested condition, the CPA strongly argued the need for conditioning short-term orders to counteract the actions of the CPUC and to maintain the integrity of the Board's GH-5-88 Decision pending restructuring of the A&S producer contracts. The CPA's views on the effect of the regulatory actions and decisions of the CPUC have been set out at section 3.3.1.1 of this Chapter.

The CPA submitted that a condition on the short-term export orders, as proposed, is the most focused, least intrusive step that the Board can take to prevent displacement of A&S' long-term gas exports. The CPA was of the view that, to be effective, the condition must preclude any deliveries into PGT of any Canadian gas destined for utilization in the Northern California market that is not gas contracted by A&S to PGT, whether such gas is exported at Kingsgate or Huntingdon, British Columbia. The CPA relied on the evidence presented at the hearing that shows that gas can be exported from Canada at Huntingdon on the Northwest Pipeline Corporation system and can be delivered into the PGT system at Stanfield, Oregon, and thus find its way through exchanges to the PG&E franchise area.

The CPA concluded that it has been shown to the Board that the CPUC actions and decisions are destroying deregulation and are abrogating the freely-negotiated contracts that formed the basis of the GH-5-88 Decision, that those actions will have a severe and detrimental effect on gas authorized to be exported under the A&S licences and that a condition on short-term orders which would prevent displacement of A&S' volumes is not only desirable, but is necessary.

With respect to the period of time during which the condition should remain in effect, the CPA asked the Board to condition all short-term export orders until restructuring of the contracts is completed and all Canadian and United States regulatory tribunals have, after due process, granted all approvals necessary to allow the restructured contracts to govern. The CPA argued that to impose any deadline whatsoever on the restructuring negotiations would tilt the balance in favour of one side of those negotiations.

3.3.3.2 Views of Interested Parties

The CPA views on Issue d) were supported by IPAC, Conwest, Pan-Alberta and B.C. and, to a certain extent, by the APMC which would prefer the suspension of ANG's interruptible service schedule but would accept, alternatively, the conditioning of short-term orders.

IPAC shared CPA's views that the Board has a wide discretion and authority to condition short-term export orders. IPAC relied on section 12 of the NEB Act which provides the Board with a broad jurisdiction to make any order, in the public interest, that by law it is authorized to make. IPAC also cited section 21 of the NEB Act as authority for the Board to vary export authorizations.

With respect to the FTA, IPAC submitted that under the provisions of the Agreement, and in particular Chapter 9, Canada remains free to determine whether and when to allow exports.

The Board is prohibited in certain circumstances from imposing a restriction on an energy good moving to the United States, but IPAC argues that the proposed condition on short-term export orders will not reduce the amount of gas flowing to California.

While Conwest did not present final argument, its witnesses fully supported the CPA application and urged the Board to condition short-term export orders as requested by the CPA.

Pan-Alberta concurred with the request of the CPA and adopted the legal arguments advanced by the Association with respect to the Board's jurisdiction to make the order sought. Pan-Alberta agreed that the Board must confirm the principles of deregulation and the concepts of sanctity of contract and minimal regulatory interference.

B.C. dealt extensively, in its final argument, with the Board's authority under the Free Trade Agreement to grant the relief sought by the CPA. With respect to the authority under the NEB Act, B.C. adopted the position put forth by the CPA, cautioning the Board, however, that it should not take action that would affect the flow of gas, whether interruptible or firm, to markets other than Northern California. That is why the Province preferred conditioning of short-term orders to amending the ANG tariff.

On the free trade issue, B.C. submitted that the granting of the relief sought by the CPA would be a legitimate exercise by the Board of its regulatory authority under the NEB Act and would not necessarily constitute a restriction on exports or imports within the meaning of the GATT or the Free Trade Agreement. In the Province's view, the requested condition would also not be a restriction by way of a minimum export price requirement.

It was the opinion of B.C. that the Free Trade Agreement has purposely left intact the energy regulatory schemes of both Canada and the United States. Chapter 9 of the Agreement recognizes the role of the NEB in Canada and of the FERC and the Economic Regulatory Administration (now Department of Energy, Office of Fossil Energy) in the United States. The role of the Board, its determination of the public interest and its administration of the surplus test of the NEB Act have not been modified by the FTA other than by the imposition of the obligation to act in a manner consistent with Articles 902, 903 and 904 of the FTA. The only changes that were made to the NEB legislation as a result of the FTA were the elimination of the "least cost alternative" price test which the Board was applying to exports and the introduction in the NEB Act of the Board's obligation to have regard to Articles 902, 903 and 904 of the FTA. Therefore, B.C. concluded that the Board would be exercising its legitimate regulatory mandate if, in determining the public interest, it considers export prices, investments made by producers and other factors related to the approval of the original long-term licences issued to A&S and concludes that the condition sought by the CPA should be granted.

B.C. did not consider the proposed condition to be a "restriction" within the meaning of the FTA. It was of the view that the FTA is very much a creation of the GATT and pointed to Article 902 of the FTA in which Canada and the United States affirm their respective rights and obligations under the GATT with respect to prohibitions and restrictions on bilateral energy goods. B.C. held the view that the provisions of the GATT, especially Article XI which is the one truly relevant to the matters before the Board, are concerned with "quantitative restrictions". Citing two decisions of international panels involving Canadian regulation of salmon and herring, one under GATT and one under the FTA, B.C. argued that an export restriction which would not be permitted under the FTA is one which favoured domestic consumption of natural gas over export consumption, which materially burdened exports as compared to domestic sales in order to discriminate as between end-users and which attempted to limit the volume of Canadian gas which is made available to the export market. B.C. was of the view that the condition proposed by the CPA does not constitute such a restriction, on the contrary, it is only attempting to preserve freely negotiated contracts under which exports to the United States are fully permitted, up to the already licensed volumes.

Citing two other cases before GATT panels related to minimum import or export prices, B.C. submitted that, by granting the relief sought by the CPA, the Board would not be taking a global action intended to prop up a domestic price nor mandate an export price which is different from the one freely negotiated between the contracting parties.

Finally, B.C. pointed to Article 905 of the FTA which provides for a consultative mechanism where energy regulatory actions are considered, by either country, to discriminate against energy goods or persons in a manner inconsistent with the principles of the FTA. There are also the provisions of Chapter 18 of the FTA which establish dispute settlement mechanisms to address the interpretation or application of any element of the FTA.

The Province argued that in light of these consultative and dispute resolution mechanisms which are available to the U.S. should it feel that any actions of the Board are inconsistent with the FTA, the Board should not hesitate to construe its subsisting regulatory powers liberally and should not be dissuaded from imposing the condition which is proposed by the CPA.

B.C. found it desirable that the Board condition the short-term export orders in the manner in which the CPA has requested. It stated that the Board should take whatever steps it can to restore the status quo during the period that commercial restructuring is taking place.

The other provincial participant, the APMC, submitted that its preferred way of ensuring proper recognition of the long-term firm arrangements underpinning the ANG system while permitting time to restructure commercial arrangements is an amendment to the tariff of ANG which would suspend the operation of the interruptible service schedule. Such a suspension of interruptible service would recognize the existence of long-term firm A&S arrangements and would prevent PGT shippers from exerting monopsony power. The APMC viewed A&S' ability to make short-term assignments under the General Terms and Conditions of the ANG tariff as sufficient to permit some flexibility in pipeline operations and to encourage maximum utilization. APMC's position with respect to access to pipeline capacity on ANG is further reviewed in subsection 3.3.4.2 of this Chapter.

Alternatively, the APMC supported the conditioning of short-term orders as requested by the CPA and IPAC as an effective means of minimizing displacement of A&S' gas and allowing time for the parties to restructure commercial arrangements.

The APMC relied on sections 19 and 20 of the NEB Act to argue that the Board is empowered to condition export orders. Section 19 allows the Board to impose conditions upon orders and subsection 21 (1) permits the Board to review, vary or rescind any order previously made. The APMC held the view that paragraph 119.01(1)(f) of the NEB Act which provides that regulations may be established indicating the terms and conditions that may be included in export orders, is not mandatory in nature and does not proscribe the types of conditions that the Board may attach to those export orders. The APMC was of the view that the Board is not limited in the imposition of conditions to those conditions identified in subsection 8(3) of the Part VI Regulations.

With respect to the operation of the NEB Act in the context of the free trade concerns, the APMC recognized that the Board must comply with Part VI, Division III of the NEB Act and give effect to the Free Trade Agreement. Pointing out that the implementation of the conditions on short-term export orders is not anticipated to change the total volume of gas exported to Northern California and that the currently licensed volumes would still be sufficient to fully utilize the export pipeline, the APMC argued that it is certainly arguable that no restriction within the meaning of the FTA would be imposed. Even assuming that the conditioning of short-term export orders would introduce a restriction on exports, subparagraphs (a), (b) or (c) of Article 904 of the FTA would not be breached and the Board would therefore not be in contravention of subsection 119.5(1) of the NEB Act. There would be no change in the proportion of the total export shipments of an energy good to the supply of that good

exported by Canada in the most recently recorded 36-month period as it is not anticipated that the total volume of gas to be exported would have to be reduced. The prices under the long-term arrangements having been established under contractual negotiations and not mandated or otherwise fixed by the Board, it could not be argued that a higher price for an export commodity than the price charged for that product domestically had been imposed. Finally, normal channels of supply or normal proportions among specific energy goods would not be disrupted by the conditioning of short-term export orders because the taking of natural gas pursuant to the long-term arrangements would be done through the historical channel of supply, at levels that would leave the proportion as between specific energy goods unchanged. The conditions of subparagraphs (a), (b) and (c) of Article 904 would be met and the restriction on exports could be introduced under the Free Trade Agreement.

None of the parties opposed to the imposition of the condition requested by the CPA - A&S, ANG, American Natural Gas Corporation ("American Natural"), Brymore, PG&E and, to a certain extent, Poco and IGI Resources Inc. ("IGI") - argued that the Board is not empowered under the Act to attach to short-term export orders the restrictions sought by the CPA. In fact, neither American Natural nor Brymore addressed directly in argument the question of the permissibility of the requested condition within the Board's current authority and Poco presumed, for the purpose of its final argument, that the Board had the jurisdiction to impose the proposed condition. IGI and Poco would prefer that the Board take no further action with respect to short-term export orders.

A&S, ANG and PG&E made submissions with respect to the free trade implications, arguing that conditioning short-term export orders as requested by the CPA would offend the Free Trade Agreement and would be contrary to those provisions of the NEB Act which provide for the implementation of the FTA. Brymore supported the position and arguments of A&S and ANG on this issue and PGT adopted the reasons advanced by PG&E.

A&S, ANG and PG&E were of the view that the condition which would be attached to the short-term exports of gas is contrary to the objectives of the FTA and to the intent of GATT. All three argued that the condition would be a restriction on exports within the meaning of the FTA and that subsection 119.5(l) of the NEB Act prevents the Board from maintaining or introducing such a restriction on exports where subparagraphs (a), (b), or (c) of Article 904 of the FTA would apply. A&S argued that the proportionality principle of subparagraph 904(a) of the FTA would be violated by the imposition of the condition. A&S was also of the view that the limitation or total prohibition of short-term exports could conceivably constitute a disruption of normal channels of supply, contrary to subparagraph 904(c) of the FTA.

ANG held the view that section 119.5 of the NEB Act prevents the Board from imposing any "restriction" - such word being unqualified - and not a "quantitative restriction" as argued by the proponents of the proposed condition. ANG did not agree that because the total volume of gas being exported to the United States might not decrease as a result of the imposition of the proposed condition, such a condition does not form a restriction or prohibition on exports within the meaning of section 119.5 of the NEB Act. The requested short-term order condition would preclude parties from exporting to the U.S., as would, in ANG's view, any restriction or prohibition to pipeline use for exports. Both these actions with respect to the export of gas would be contrary to section 119.5 of the NEB Act. ANG also argued that by preventing displacement of long-term A&S deliveries by lower priced short-term or spot gas, the Board would be setting a minimum export price contrary to Articles 407 and 902 of the FTA. ANG further submitted that, as a consequence of the 1990 amendments to

section 118 of the NEB Act resulting from the implementation of the FTA, the price of the exported energy good is no longer a relevant consideration in the exercise of the Board's discretionary powers. The broad jurisdiction conferred on the Board by sections 12 and 19 of the NEB Act must be read in light of the specific considerations that the Board may properly take into account under section 118 and ANG argued that an export condition which sets a minimum price cannot be imposed pursuant to section 19 of the Act.

PG&E was also of the opinion that the proposed condition would set a minimum export price contrary to the FTA. PG&E argued that the condition, like any export licensing practice, is a restriction within the meaning of GATT and that the three conditions of Article 904 of the FTA would not be met. PG&E submitted that retaliation against the actions of the CPUC does not justify the imposition of an illegal export restriction. In PG&E's view, the proposed condition is contrary to deregulation, is interventionist and premature. It is also discriminatory because it would, in effect, only permit exports from one aggregator, A&S, under one type of supply contract and would prevent others from exporting.

On the question of whether it is desirable for the Board to attach the proposed condition to all short-term export orders, the opponents were unanimous in questioning the effectiveness of such a measure. The parties doubted whether restricting short-term interruptible exports would necessarily restore and maintain the high level of A&S exports to Northern California. On the contrary, those opposed to the condition feared that the Pacific Northwest markets, incremental markets in Northern California, that portion of the UEG market which cannot be supplied by PG&E system gas and other non-core customers who can buy direct, would turn to the U.S. spot gas market if they cannot be supplied by Canadian short-term interruptible exports and export revenues would therefore be lost. Furthermore, the U.S. market in general would begin to question the reliability of Canadian supplies if regulatory actions interfere with the flow of authorized exports.

ANG and Brymore also submitted that there is no compelling evidence before the Board of the displacement of the A&S sales by short-term interruptible exports. Any reduction in the recent A&S deliveries to Northern California may be attributable to factors other than displacement by other Canadian sales, such as weather conditions, market restructuring or competitive U.S. sourced spot gas. ANG added that a restriction on interruptible exports would result in higher unit transportation costs for shippers remaining on the export pipeline system. This position was also expressed by Brymore.

ANG and Poco were of the view that the negotiations which are being carried on between Alberta, B.C. and the CPUC under the Energy Consultative Mechanism to resolve the Canada-California conflict and the commercial renegotiations involving A&S with its purchaser, PG&E, as well as A&S with its Canadian producers, should be permitted to yield their results without regulatory interference from this Board. PG&E had the same view with respect to the commercial negotiations to restructure gas sales to California; regulatory interference would be counter-productive.

All those opposing the CPA application agreed that, should the Board find that some restriction on short-term interruptible exports is warranted, any resulting condition should be limited to the displacement of PG&E volumes to Northern California. Sales to the Pacific Northwest and incremental sales to Northern California should not be affected. Continued access to the Pacific Northwest market was IGI's main concern and it feared that suspension of interruptible service on ANG as requested by the APMC would have a negative impact on sales into that market. IGI relied on the support of B.C., ANG and the CPA to argue against the imposition of restrictions on short-term sales to the Pacific

Northwest region. It pointed to sections 62 and 67 of the NEB Act as providing authority for the Board to limit any restriction to interruptible service on ANG to service to Northern California.

Although the parties opposing the CPA application preferred no restriction whatsoever on short-term interruptible exports to Northern California, most stated a willingness to accept continuation, until completion of commercial restructuring, of the Board's interim order MOI-1-92 rather than the imposition of the condition proposed by the CPA. They argued that the MOI-1-92 restriction is more focused and flexible than the requested condition and permits exports to markets other than Northern California and sales which do not displace the A&S gas.

Brymore and PG&E also feared that any action by the Board in response to the CPA application would establish the precedent that any party not directly involved in an export sales contract might seek the review of an export authorization for reasons unrelated to the appropriate regulation of exports.

Finally, A&S and PGT doubted whether the imposition of the proposed condition would effectively solve either the short-term or long-term problems facing the Canadian producers. Those problems would be solved by the renegotiation of the contracts and by the restructuring of the export arrangements.

3.3.3.3 Views of the Board

The Board is of the view that it has the necessary powers under section 19 of the NEB Act to attach to short-term export orders, issued pursuant to the Part VI Regulations, the condition proposed by the CPA and which would prohibit exports of any Canadian gas destined for utilization in the Northern California market that is not gas presently contracted by A&S for sale to PGT. The Board is also of the opinion that it can, pursuant to section 21 of its Act, vary existing short-term export orders by adding the requested condition to those orders.

While the Board recognizes that the Governor in Council may, under paragraph 119.01(l)(f) of the NEB Act, make regulations respecting the terms and conditions that may be included in gas export orders, it is of the opinion that its statutory powers, under subsection 19(l) of its Act, to make conditional orders, is sufficient authority to impose the condition requested by the CPA in short-term export orders. Section 19 is a general legislative provision applicable in respect of certificates, licences or orders issued by the Board which is not restricted by any other provision of the Act or the regulations. With respect to section 21 of the NEB Act, the Board agrees that it has unfettered discretion to review and vary any of its decisions or orders and it relies on the Federal Court decision in the GH-3-86 Review in this regard.

With respect to the Free Trade Agreement and the provisions of the NEB Act related to that Agreement, the Board has been convinced by the arguments of the CPA, IPAC and B.C. that the imposition of the proposed condition would not breach any of the Board's obligations.

The Board does not consider an export order condition which prevents displacement of gas sales already authorized for export and which can be transmitted, unhindered, by pipeline to the U.S., at freely negotiated prices, to be a restriction within the meaning of the FTA. The total volume of gas flowing to the U.S. from Canada will not be restricted; prices are not dictated by the Board but are set by the parties through negotiation; and Canadian purchasers will not be favoured by the imposition of

the condition. Therefore, the Board finds that the conditions of subparagraphs (a), (b) and (c) of Article 904 of the FTA would be met. In particular, by preventing displacement of long-term firm volumes by short-term interruptible sales, the Board is not reducing the proportion of the total export shipments of gas made available to the U.S. relative to the total supply of gas to Canada. The requested condition is not imposing a higher price for exports than the price charged domestically for gas. Finally by limiting the displacement of long-term firm exports by short-term interruptible exports, normal channels of supply to the U.S. would not be disrupted.

The Board agrees with those parties requesting the imposition of a condition that, in exercising its jurisdiction by imposing such a condition, the Board would not be acting contrary to the provisions of the FTA. The Board therefore finds that it is permissible under its current authority to condition short-term export orders as proposed by the CPA, and as supported by IPAC, the APMC and B.C.

The Board finds that it is desirable to condition short-term orders as proposed by the CPA for the reasons stated in the Views of the Board with respect to Issues a), b) and c). That is, the CPUC's regulatory actions have: substantially changed the evidentiary underpinnings of the Board's GH-5-88 Decision; adversely affected the Canadian public interest; created a bias against Canadian interests in the process of commercial restructuring; and adversely affected the time required for parties to seek fair and equitable settlements.

The order will remain in effect for a period sufficient to allow for fair and equitable contractual arrangements to be negotiated by all affected parties and until all necessary regulatory approvals are in place for such new arrangements.

3.3.4 Issues e) and f):

> whether access to pipeline capacity on ANG does or should take into account existing long-term contractual arrangements for the sale of Canadian gas to California markets in view of the potential consequences of recent regulatory actions and decisions taken in the United States of America; and
>
> whether amendments to ANG's tariff are required to address those issues raised in paragraph e) or any other effects on the transportation and sale of Canadian gas as a result of the regulatory actions and decision take in the United States of America and, if so, for what period of time should these changes to the tariff remain in effect.

3.3.4.1 Views of the CPA

The CPA stated that the Board must take into account existing long-term contractual arrangements for access to pipeline capacity on ANG because of the regulatory interference of the CPUC with contracts. However, it was the CPA's view that amendments to ANG's tariff to address potential consequences of regulatory actions in California were less desirable than a condition on short-term export orders because a tariff amendment could affect sales to markets other than Northern California.

The Association was supportive of any measure which would prevent the displacement of A&S' sales to PG&E and would, therefore, not oppose an amendment to ANG's tariff which would have this effect. The CPA argued that, to be effective, any tariff amendment should also prevent buy/sell arrangements which could result in such displacements. Finally, the CPA stated that any measure

which the Board might adopt relating to ANG's tariff should be in place until restructuring is completed.

3.3.4.2 Views of Interested Parties

IPAC and APMC argued that access to pipeline capacity on ANG should take into account existing long-term arrangements because of the firm transportation rights acquired by A&S to facilitate the sale of its gas to PG&E via the PGT system. IPAC submitted that the individual producers which dedicated reserves to underpin the A&S export licences should benefit from the transportation rights acquired by A&S on their behalf.

B.C. stated that if the Board were to implement any amendments to the ANG tariff, long-term contractual arrangements should be considered and any tariff amendment should prevent buy/sell arrangements until the commercial restructuring has been completed.

It was the position of the APMC that an amendment to the ANG tariff to suspend the interruptible service schedule should be adopted by the Board to ensure that existing long-term firm arrangements of A&S are recognized until restructuring is completed. In the APMC's view, this measure is required because ANG's current tariff permits actions in California to determine which gas flows on this system. In order to get transportation service on ANG, a potential shipper has to demonstrate that it has downstream capacity on PGT. Furthermore, the APMC pointed out that ANG agreed that more capacity for interruptible service would become available as a result of A&S' capacity not being fully utilized and this additional interruptible capacity could result in displacement of A&S' sales.

IPAC supported the APMC's proposal as a second-best solution.

ANG, Brymore, IGI and Poco stated that the Board should retain the interim measures only if it was convinced that some actions were required.

Brymore and PG&E argued that access to pipeline capacity already takes into account long-term contractual arrangements for the sale of Canadian gas to California markets through A&S' firm service on ANG and that no tariff amendments on ANG were required. However, PG&E added that access to pipeline capacity should be on the basis of defined tariffs and should not be conditional upon certain performance under sales contracts.

Except for the APMC, no interested parties argued for any restrictions which would preclude the exportation of natural gas to incremental markets in Northern California or the Pacific Northwest.

3.3.4.3 Views of the Board

The Board finds that the CPUC actions infringe on its exclusive Jurisdiction in regard to the regulation of transportation access on ANG. A criterion in the GH-5-88 proceeding was that transportation arrangements would be in place to transport the A&S gas to the Northern California market. This included the A&S firm transportation contract for the provision of service on the ANG pipeline system.

The Board is of the view that the CPUC actions would significantly and progressively reduce the gas takes by PG&E from PGT, and consequently by PGT from A&S and its Canadian producers.

Consequently, there would be a significant reduction in firm capacity utilization on ANG. Thus, excess capacity for interruptible transportation on the ANG system would be created due to the reduction in the demand for firm transportation service by A&S. The Board believes that these effects would be brought about, not by market factors, but as a direct result of unilateral and overreaching intervention by the CPUC to overturn the existing, long-term, bilateral commercial arrangements to supply gas to Northern California.

The CPUC actions constitute a major change in the business environment for the ANG pipeline system. In the Board's view, renegotiation of the related contractual arrangements require more time than is currently permitted by the CPUC orders. Accordingly, the Board is of the view that amendments to ANG's tariff are required to prevent the artificial creation of interruptible capacity on ANG and that such amendments should remain in place until arrangements, satisfactory to all of the parties involved, are completed.

3.3.5 "Incrementality Test"

On the last day of the hearing, the Board brought to the attention of parties and sought comments on Article 17, paragraph (i) of the 1985 Agreement on Natural Gas Markets and Prices which provides for the elimination of the "incrementality test". This test was introduced in 1984 when the Government of Canada established its natural gas export policy to allow negotiated prices in November of that year. The Board solicited the views of the parties as to whether the imposition of a condition on short-term gas export orders as proposed by the CPA would constitute, in fact, the reimposition of the "incrementality test".

The incrementality test referred to in the 1985 Agreement was embodied in a 2 October 1984 NEB document entitled *Regulatory Procedures and Information Requirements for Applicants Filing for Short-term Natural Gas Export Orders*. One such requirement, at item 7, read, in part, as follows:

> Exporters must demonstrate that the sales are truly incremental and will not displace other Canadian gas sales, directly or indirectly.
>
> Applicants will be expected to provide the Board with evidence that the proposed exports are new Canadian sales and that the segment of the U.S. market proposed to be served is not currently being served by Canadian gas.

The 1985 Agreement provides, at Article 17(i) that:

> Effective November 1, 1985, the Government of Canada will take appropriate steps to amend its existing policy on short-term export sales of natural gas. Specifically, the "incrementality test" shall be eliminated.

3.3.5.1 Views of the Interested Parties

The Board received written comments from the CPA, ANG, Poco, the APMC and B.C. as well as reply comments from the CPA.

The parties who submitted comments in favour of conditioning short-term export orders, i.e., the CPA, the APMC and B.C., argued that the condition proposed by the CPA would not resurrect the incrementality test which was eliminated by the 1985 Agreement. However, both the APMC and B.C.

recognized that the condition resembles the incrementality test. The CPA did not make such an admission and submitted that implementation of the requested condition would not effectively reinstitute an incrementality test.

All three parties supporting the condition relied upon Clause 21 of the 1985 Agreement which states that:

> The Government of Canada has broad responsibilities to ensure that trade among the provinces and between Canada and its foreign trading partners is conducted in a manner which will provide benefits for all Canadians. Nothing in this Agreement shall limit Canada's power or its ability to meet its responsibilities in relation to interprovincial and international trade.

The proponents of the short-term export order condition argued that Clause 21 should override Clause 17 for reasons of public interest. For the APMC, the Canadian public interest requires a fair and orderly transition to a market-based environment and reliance on commercial decisions. B.C. argued that the Government of Canada must ensure that international trade is conducted in such a manner as to provide benefits to all Canadians. B.C. considered it in the public interest that existing contracts not be abrogated and that the considerable expenditures incurred by the Canadian producers be recovered. The CPA submitted that Canada's responsibilities in relation to international trade, as recognized in Clause 21 of the 1985 Agreement, include the maintenance of Canadian energy policy as reflected in the Market-Based Procedure, and the protection of sanctity of contracts.

All the parties stressed that the measures sought by the CPA would be temporary until restructuring of the commercial arrangements had taken place and used this fact as a further argument for overriding Clause 17 of the 1985 Agreement. All three also reminded the Board of its position in its *Reasons for Decision, Manitoba Oil and Gas Corporation Application Dated 25 May 1987, as Amended for Orders Directing TransCanada PipeLines Limited to Receive, Transport and Deliver Natural Gas and Fixing Tolls, MH-1-87, September, 1987* ("MH-1-87") concerning the 1985 Agreement. The Board had held that the Agreement was a political document, the intent of which was not easy to discern and that, for this reason, considerable weight should be given, in examining that intent, to the testimony of the signatories to the Agreement.

The APMC added that its proposal to amend the ANG tariff instead of conditioning short-term export orders was intended to address a structural problem concerning pipeline access and that it did not raise the problem of the incrementality test.

Finally, the CPA pointed out that the A&S contract which underpinned the GH-5-88 application had been freely negotiated by the parties after the implementation of the 1985 Agreement and had taken into account the market restructuring policies developed by the CPUC in the 1986-1988 time period. ANG and Poco which both opposed the short-term export order condition applied for by the CPA expressed the view that such a condition would contravene Clause 17 of the 1985 Agreement as well as the intent and spirit of that Agreement. ANG added that any indirect restriction through tariff amendments would also contravene the principles and intent underlying the elimination of the incrementality test which were meant to foster gas-on-gas competition and non- discriminatory market access. Poco reminded the Board that the parties now advocating restriction on short-term export orders to California - the CPA, IPAC, Alberta through the APMC, and B.C. - were all, at the time of deregulation, endorsing Clause 17 of the 1985 Agreement.

3.3.5.2 Views of the Board

None of the parties who elected to respond to the Board's question, have attempted to establish that the question of the incrementality test is not relevant to the CPA application. In fact, none have strongly argued that the condition requested by the CPA would not have the effect of reinstituting some sort of incrementality test. On the contrary, the parties have argued that the Canadian public interest in general and the provisions of Clause 21 of the 1985 Agreement, in particular, justify and authorize the overriding of Clause 17.

The Board is of the view that the condition which the CPA requests to be attached to short-term export orders would in fact reinstitute the incrementality test. Its purpose is obviously to prevent that segment of the U.S. market currently being served by Canadian gas from obtaining access to a new source of Canadian gas. That is exactly what the export policy of July 1984 was intended to achieve and Clause 17 of the 1985 Agreement amended this policy and set aside the "incrementality test".

The Board is also of the opinion that amending the tariff of ANG to restrict availability of interruptible service, while appearing to be somewhat contrary to the spirit of the 1985 Agreement which was intended to attain significantly freer market access, would not result in any specific breach of Clause 17 or of any other provision of the 1985 Agreement which deals essentially with a market-oriented pricing regime for gas.

The Board has concluded that Clause 21 of the 1985 Agreement, which was relied upon by all the proponents of the proposed condition, is a statement of general application which confirms that the Federal Government's responsibilities with respect to energy regulation have not been affected by the 1985 Agreement. The Board has also determined that, in accordance with Clause 21 of the 1985 Agreement, its jurisdiction over gas exports has remained unchanged and that it still has the responsibility to determine that these exports are in the Canadian public interest.

In conformity with its earlier decision, especially the one in MH-1-87, the Board has relied on the evidence and arguments of the signatories to the Agreement, in this case the APMC as representative of Alberta, and B.C., to ascertain the scope and intent of the 1985 Agreement with respect to the actions applied for by the CPA.

Those elements of the Canadian public interest that the Board wishes to maintain and protect are a fair and orderly transition to renegotiated prices and other terms between buyers and sellers. The recovery of investments made by producers to provide a supply of gas to California is also a legitimate factor in the determination of the public interest. Furthermore, the Board has noted the temporary nature of the condition which is not intended to last beyond the negotiated restructuring of the contractual arrangements between the Canadian producers and the California buyers.

The Board has therefore concluded that the Canadian public interest, the provisions of Clause 21 of the 1985 Agreement, the specific circumstances of the Northern California problem and the temporary nature of the relief sought by the CPA, all argue in favour of the imposition of limits on short-term export orders even though this would, in effect, reintroduce the incrementality test for a segment of the Northern California market.

Chapter 4
Summary and Conclusions

The Board is concerned and dismayed at the adverse effects on Canada of the CPUC's actions respecting utility gas procurement practices and transportation service. These effects relate to:

- the stranding of financial commitments made by Canadian producers to develop a long-term, secure supply of competitively priced gas for California, having placed reliance on representations made by California regulators as to the continuance of the regulatory regime in effect at the time these commitments were made;

- the inadequacy of the transition period contemplated by the CPUC which could be less than 12 months; and

- the Commission's encroachment on the jurisdiction of regulatory authorities outside the boundaries of the State of California, in particular the jurisdiction of this Board.

Canadian Financial Commitments Stranded

The existing chain of contracts between PG&E, PGT, A&S and Canadian producers was negotiated under a CPUC regulatory regime which encouraged end-users in PG&E's franchise area to purchase gas from PG&E which would, in turn, obtain a substantial part of its total supplies and all its Canadian gas through its aggregator A&S. It was under this regulatory environment, which held out the promise of secure and dependable markets, that Canadian gas producers undertook major commitments to finance the development of the additional gas supplies in Canada purported to be needed and entered into long-term gas sales and purchase contracts with A&S to serve the Northern California market.

This was the context in which the Board conducted its GH-5-88 proceeding and made its Decision, rendered in May 1989, to issue the new Licence GL-111 to enable A&S to continue to supply the Northern California market with a secure, long-term, contracted flow of Canadian gas to the year 2005. The Board notes that, in the GH-5-88 hearing, both the CPUC and the CEC submitted letters strongly endorsing A&S' application to extend its licence to the year 2010.

Within two years of the Board's GH-5-88 Decision, while Canadian producers were in the process of fulfilling their contractual commitments to find and develop new gas supplies to serve the Northern California market, the CPUC adopted a diametrically opposite view of the appropriate gas market structure. It has opted for a structure which is inimical to the contractual arrangements so recently extended and endorsed by provincial/state regulators in Alberta, B.C. and California and by federal regulators in Canada and the U.S.

By a series of decisions and rulings (See section 2.4.2) the CPUC has:

- caused PG&E to renegotiate its gas supply contracts with Canadian producers through its affiliated companies, PGT and A&S, to reduce minimum takes and improve flexibility by 31 December 1991;

- changed from a position, at the time of the GH-5-88 proceeding, of favouring the purchase of gas by all customers from the gas distribution utilities, to one favouring widespread direct purchase and transportation;

- directed UEG departments, which had relied on gas utilities such as PG&E for the major portion of their gas requirements, to reduce the proportion of their purchases from such gas utilities from 65 percent to zero over a six-year period; and

- applauded an Access Agreement negotiated by PG&E and its Canadian suppliers, which provides for some direct purchases by California end users over a three-year transition period ending 1 August 1994, and a little over a year later rejected this Agreement in favour of capacity brokering to be implemented as early as 1 October 1992.

The evidence in this proceeding is that these actions of the CPUC will drastically reduce the takes of gas from Canadian supplies developed on the basis of long-term contracts which had been negotiated in good faith, in the expectation of the continuance of a California regulatory environment established by the CPUC.

Inadequate Length of Transition Period

While regulatory change is a risk and a fact of life in the evolving North American gas market, regulators need to be cognizant of the fact that such changes potentially impose costs on parties who have negotiated contractual arrangements in good faith, based on the expectation that the regulatory policies then in effect would provide a measure of stability and reliability. Consequently, as a matter of fairness and equity, regulators have been inclined to provide an appropriate framework, including a sufficient period of time, for the parties they regulate and other affected parties to react and adjust to changes in the regulatory regime in which they must do business.

In a Canadian context, for example, this Board, in its ruling on the self-displacement issue on the TransCanada pipeline system (i.e., the replacement of gas, purchased by LDCs under contract with TransCanada, with gas purchased directly from producers), stated that, in pursuing its objective of open access transportation,

> ...the Board has taken measures to ensure that all parties are treated fairly and equitably with respect to the ... terms and conditions of transportation.
>
> (RH-1-88 Phase I. p.6)

Among these measures was the denial of self-displacement by domestic gas distributors for a transition period of three years. The effect of this was to give consumers and producers time to renegotiate the provisions of existing long-term contracts prior to the implementation of open access on the TransCanada system.

The transition period contemplated by the CPUC, ending as early as 1 October 1992, is, in the Board's view, almost certainly too short to allow time for parties to arrive at fair and equitable settlements in private contractual negotiations.

Encroachment on Canadian Jurisdiction

For the contractual and regulatory changes to occur within the timeframe contemplated by the CPUC, that Commission must presume that this Board would simply acquiesce by taking any necessary complementary regulatory action in Canada relating to export authorizations and transportation access to the ANG pipeline without taking any account of the Canadian public interest.

The Board recognizes that licences to export gas are permissive and any action the Board might take would not change that basic licence characteristic. However, the Board cannot stand idly by when the regulatory actions of others adversely affect the basis upon which it was persuaded to issue a licence. This is so in the case at hand, where contractual arrangements negotiated in good faith underpinning a licence are effectively abrogated by regulatory actions which do not provide sufficient time and a fair negotiating environment for affected parties to adjust and restructure these commercial arrangements.

The CPUC's actions also infringe on the Board's jurisdictional mandate to regulate transportation access on ANG. Because the CPUC actions would significantly and progressively reduce the gas takes by PG&E from PGT and consequently by PGT from A&S and its Canadian producers, there would, as a consequence, be a significant reduction in firm capacity utilization on ANG. Thus, capacity for interruptible transportation would artificially be created on the ANG system due to the reduction in the demand for firm transportation service by A&S. These effects would arise, not because of market factors, but as the direct result of the CPUC regulatory changes which affect the existing long-term contractual arrangements to supply gas to Northern California. It would not be in the Canadian public interest to allow changes to existing transportation arrangements on ANG to occur until appropriate transitional arrangements are in place.

This Board's policy and practice is to allow and encourage the freest possible operation of gas markets, national and international. In seeking to uphold transactions based on contractual arrangements negotiated in good faith between buyers and sellers, it has provided open access transportation on pipelines. However, the Board's commitment to a freely-functioning gas market does not imply or entail that it automatically take regulatory actions parallel to and supportive of regulatory actions in other jurisdictions, if such actions would have the effect of overturning, at short notice and without an adequate transitional period, negotiated contractual arrangements on which this Board placed reliance in its decisions.

Chapter 5
Decision

The Board has decided to prevent the displacement of the long-term firm gas supply of A&S and its producers to Northern California by exports authorized under short-term orders and transported under interruptible arrangements, and to prevent the underutilization of capacity on the ANG pipeline system under firm transportation contracts .

Specifically the Board is rescinding its interim orders and is issuing orders to:

- immediately vary all short-term export orders to add a condition that precludes exports at Kingsgate and Huntingdon, British Columbia, of Canadian gas destined for utilization in the Northern California market that is not gas presently contracted by A&S for sale to PGT and;

- immediately suspend interruptible transportation service for the delivery of gas to the Kingsgate, British Columbia, export point and the assignment provisions of ANG's Gas Transportation Service Document.

These orders will remain in effect for a period sufficient to allow for fair and equitable contractual arrangements to be negotiated by all affected parties and until all necessary regulatory approvals are in place for such new arrangements. If an understanding or agreement is reached between the CPUC and the Alberta and B.C. governments, the Board will solicit comments from interested parties to the GH-R-1-91 proceeding on its implications for this decision.

In issuing the order pertaining to the export of gas, the Board is satisfied that it is permissible within the Board's current authority and is consistent with the Board's obligations under the FTA.

In issuing the order pertaining to traffic, tolls and tariffs, the Board will grant leave upon application by shippers who can satisfy the Board that the gas to be delivered at Kingsgate, British Columbia, is destined for utilization in the Pacific Northwest or the Southern California market areas in the United States.

The Board finds that no unjust discrimination flows from the tariff order. The Board has determined that it would be inappropriate to allow interruptible transportation service to be substituted for firm transportation service as a result of the forced displacement of long-term contractual arrangements on ANG and that such substitution would be contrary to the public interest.

In arriving at its decision, the Board confirms and reiterates that the continuation and extension of Licence GL-99 by Licence GL-111 was authorized by the Board:

- in accordance with the Market-Based Procedure which was established by the NEB after the hearing held pursuant to NEB Order GHR-1-87 and which implemented Canadian national energy policy based on the premise that the marketplace will generally operate in such a way that Canadian requirements will be met at fair market prices;

- in recognition of long-term firm supply contracts which Canadian producers of natural gas entered into with A&S in reliance upon representations by A&S that the dedication of reserves and lands by producers would be to serve PG&E markets in Northern California at prices competitive with the delivered cost of alternate energy at the point of consumption in the marketplace; and

- in reliance upon representations by A&S, PG&E, the CPUC and CEC to the effect that the licence extension, based as it was on the A&S/Canadian producer contracts, was necessary to ensure that a long-term secure supply of Canadian gas would be available at prices which are competitive in the PG&E marketplace subject to the market-driven regulatory framework encouraged by the CPUC.

The Board makes no finding with respect to the actions of the CPUC in respect of the intent of Canadian and United States energy policy or the Canada-United States Free Trade Agreement. This Board does not believe it is the proper authority to adjudicate on these matters.

Chapter 6
Disposition

The foregoing chapters, together with Orders MO-2-92 and TG-5-92, constitute our Reasons for Decision and Decision on this matter.

R. Priddle
Presiding Member

J.-G. Fredette
Member

A. B. Gilmour
Member